

GASB and Audit Update

May 2013

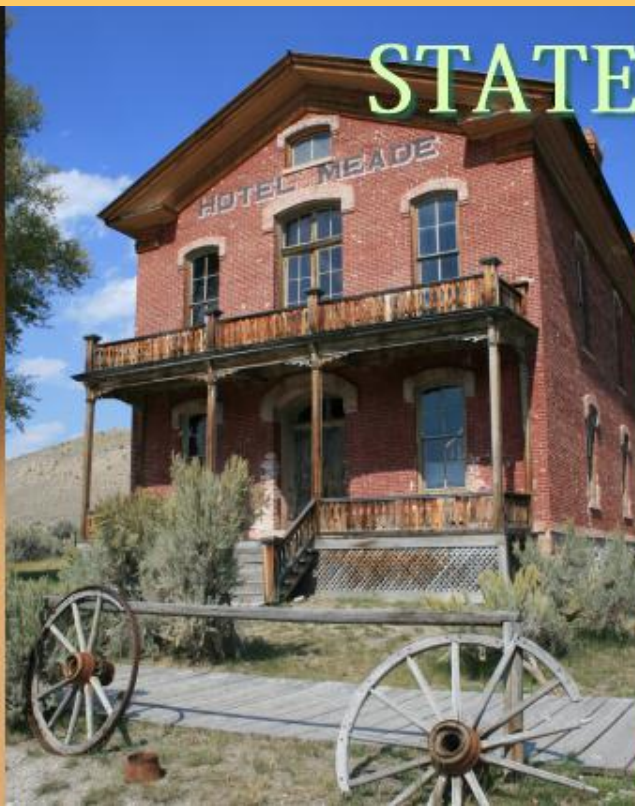
Eric S. Berman, MSA, CPA, CGMA

Brown Armstrong Accountancy Corporation

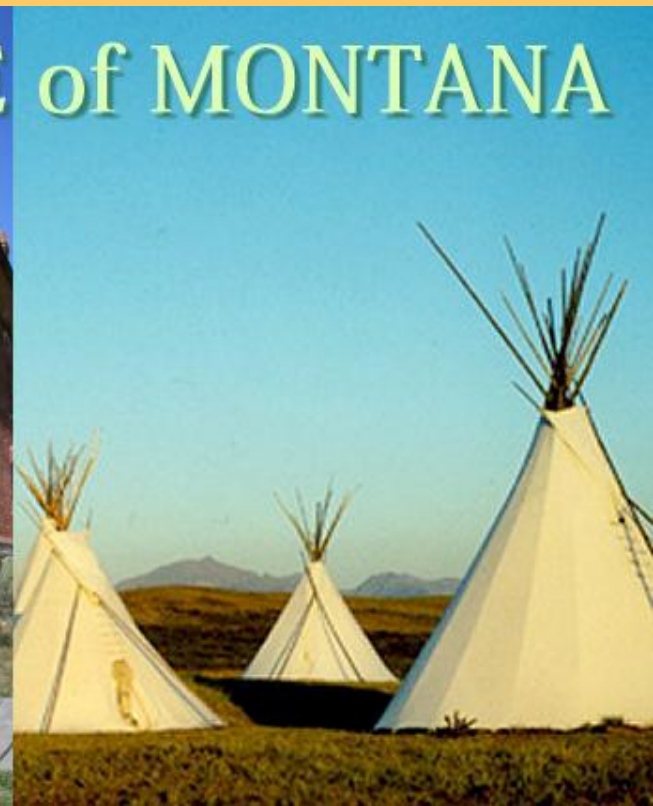
Pasadena, California



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Agenda

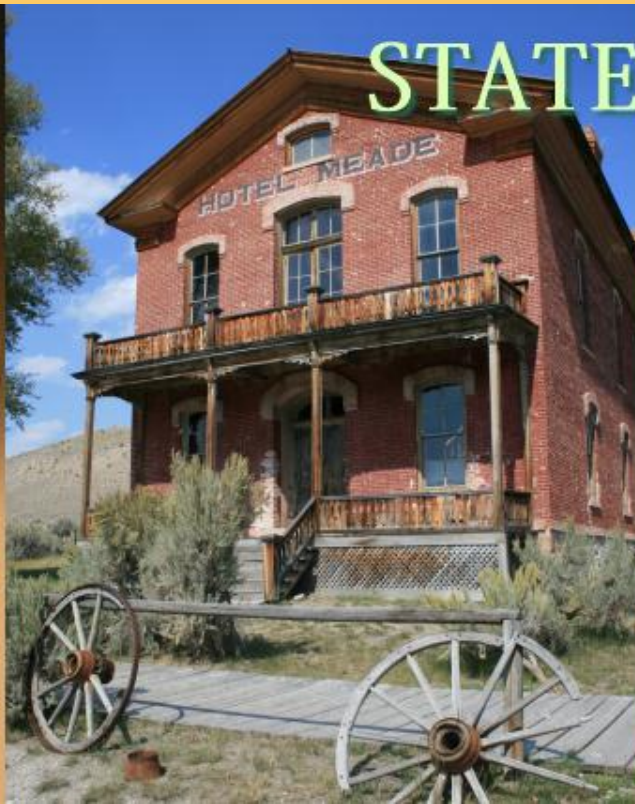
- Practical Application of GASB Standards 60 through 70 (*new*) (12 hours+/-)
- Audit Update (4 hours+/-)



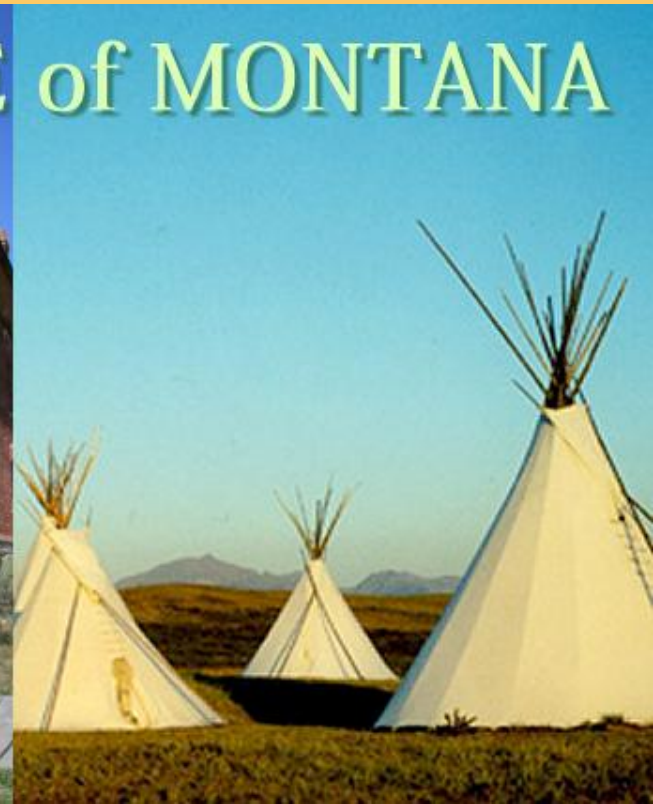
Practical Application of GASB Standards 60 – 70 (new)



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GASB Update

- Implementation Calendar
- GASB Standards Most Important
 - GASB 60 – Service Concession Arrangements
 - GASB 61 – Component Unit Guidance
 - GASB 63- Inflows / Outflows, Net Position
 - GASB 65 – Deferred Inflows & Outflows
 - GASB 67 and GASB 68 Pension Standards *including the upcoming Technical Correction on Pensions due to be released shortly*
 - GASB 69 - Combinations
 - GASB 70 – Financial Guarantees - *NEW*
 - Exposure drafts
 - The latest on other projects!

Implementation Dates

Statement	Topic	Date	Fiscal Year
60	Service Concession Arrangements	Financial statements for periods <i>beginning</i> after 12/15/11	July 1, 2012 – June 30, 2013
61	Component Units	Financial statements for periods <i>beginning</i> after 6/15/12	July 1, 2012 – June 30, 2013
62	Codification	Financial statements for periods <i>beginning</i> after 12/15/11	July 1, 2012 – June 30, 2013
63	Statement of Net Position	Financial statements for periods <i>beginning</i> after 12/15/11	July 1, 2012 – June 30, 2013



Implementation Dates

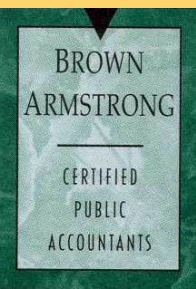
Statement	Topic	Date	Fiscal Year
65 – NEW	Items Previously Reported as Assets and Liabilities	Financial statements for periods <i>beginning</i> after 12/15/12 – likely to implement though with GASB 62 – 1 year earlier	July 1, 2013 – June 30, 2014
66 – NEW	Technical Corrections - 2012	Financial statements for periods <i>beginning</i> after 12/15/12 – likely to implement though with GASB 62 – 1 year earlier	July 1, 2013 – June 30, 2014

Implementation Dates

Statement	Topic	Date	Fiscal Year
GASB-67	Financial Reporting for Plans – An amendment of GASB-25	Fiscal years <i>beginning</i> after June 15, 2013 – retroactive aspects	July 1, 2013 – June 30, 2014
GASB-68	Accounting and Financial Reporting for Pensions – An amendment of GASB-27	Fiscal years <i>beginning</i> after June 15, 2014 – retroactive aspects	July 1, 2014 – June 30, 2015
GASB-69	Government Combinations and Disposals of Government Operations	Periods <i>beginning</i> after December 15, 2013	July 1, 2014- June 30, 2015
New – GASB-70	Accounting and Financial Reporting for Nonexchange Financial Guarantee Transactions	Periods <i>beginning</i> after June 15, 2013	July 1, 2013 – June 30, 2014

Implementation Calendar

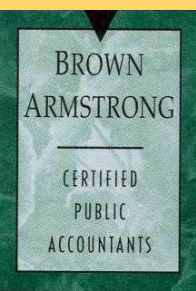
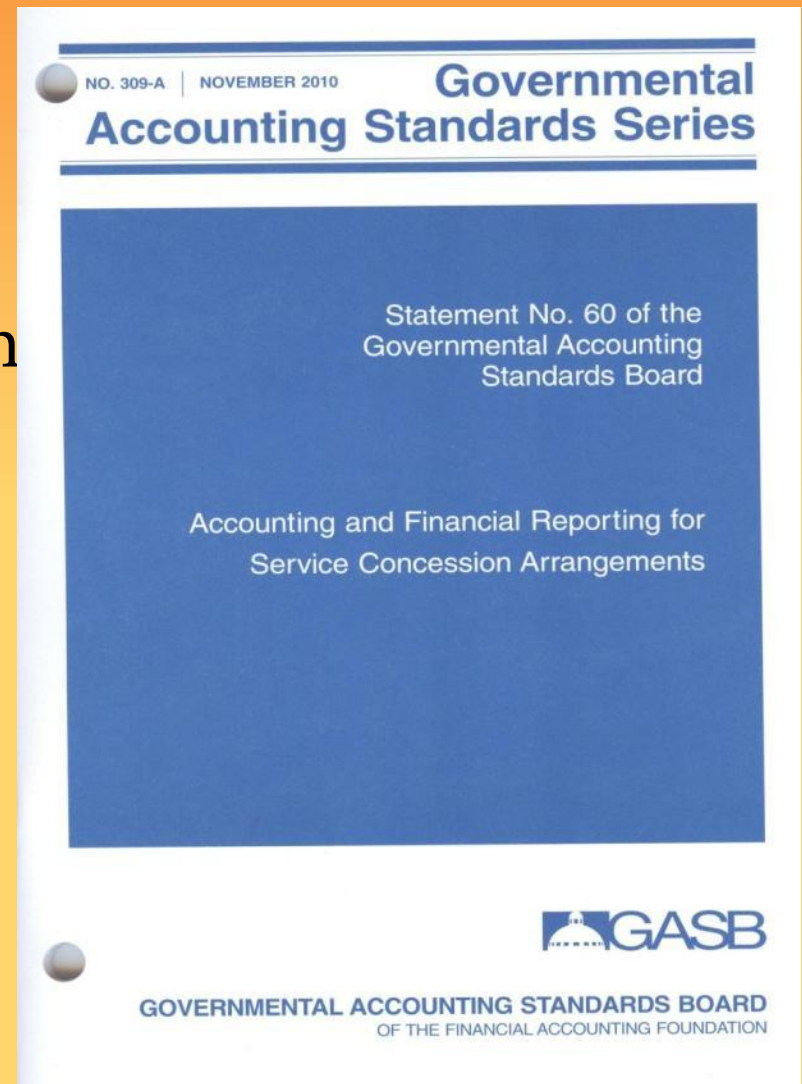
2012-2013	2013-2014	2014-2015
60	65 (unless w/ 62)	69
61	66 (unless w/ 62)	68
62	67	
63	Guarantees 70	



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Statement No. 60

- Accounting and Financial Reporting for Service Concession Arrangements



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GASB 60- SCAs – Key Points

- SCAs are a type of public / private partnership *or* public / public partnership
- Needs
 - Transferor Government
 - Has rights and can impose obligations through the use of infrastructure or facilities
 - Operator
 - Can be another government or a private entity

GASB 60- SCAs – Key Points

- Terms of the SCA may include
 - Payments from the operator to the government for the right to build, operate and collect user fees on infrastructure or public asset
 - May include revenue sharing arrangements

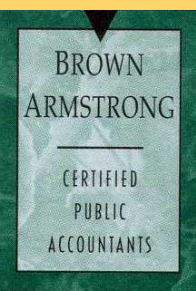


GASB 60- SCAs – Key Points

- SCAs exist when all criteria are met:
 - Transfer must be between a government and *either* another government or a private entity that will serve as an *operator*
 - Right and obligation is conveyed to provide public services through the use and operation of a capital asset in exchange for *significant consideration*.
 - Can be up front payment or installments, a new facility or a betterment to an existing facility

GASB 60- SCAs – Key Points

- SCAs exist when all criteria are met:
 - The operator collects and is compensated by fees from third parties
 - The transferor government is entitled to a residual interest at the end of the SCA
 - The transferor government has the ability to modify / approve the services that the operator provides, to whom it is provided and the prices / rates charged



GASB 60- SCAs – Key Points

- Reporting is only on full accrual financial statements (**not in governmental fund statements**)
- If provisions are met then:
 - Transferor government continues to report capital asset for facility
 - If new facility, capital asset reported by transferor at fair value along with any contractual obligations
 - Deferred Inflow of Resources reported as the difference

GASB 60- SCAs – Key Points

- Liability is at present value of the obligation when
 - Contractual obligation relates to the facility (capital improvements, O&M, insurance etc.)
 - Could relate to a minimum level of service provided by the government for the facility (e.g. police / fire presence)

GASB 60- SCAs – Key Points

- Capital Asset rules carry forward unless the asset is required to be returned to the government in its original or better condition
 - Improvements capitalized / depreciated
- **Deferred Inflow of Resources** recognized and reduced / revenue recognized systematically over life of arrangement
 - If liability is set up for future services that need to be provided – reduced as services provided

GASB 60- SCAs – Key Points

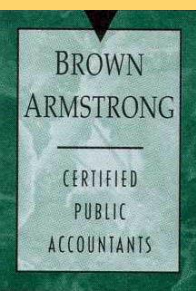
- What about up front or installment payments from operator?
 - Record at present value as an asset
 - Contractual obligations as liabilities
 - **Deferred inflow of resources as difference**
 - Revenue recognized as deferral reduces

GASB 60- SCAs – Key Points

- What about governmental operators?
 - Right to access facility is an intangible asset per GASB-51
 - Any improvements increase the intangible asset
 - Amortization is over the life of the agreements
 - If specified condition is needed upon return
 - If asset not in the condition
 - If amount to restore is estimable
 - Liability declared then

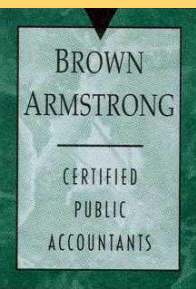
GASB 60- SCAs – Key Points

- Revenue Sharing Arrangements
 - Transferor government only reports revenue that accrues to them
 - If revenue sharing amount is fixed
 - Amounts should be reported at present value by transferor government and governmental operator
- Transition – now– restate prior periods

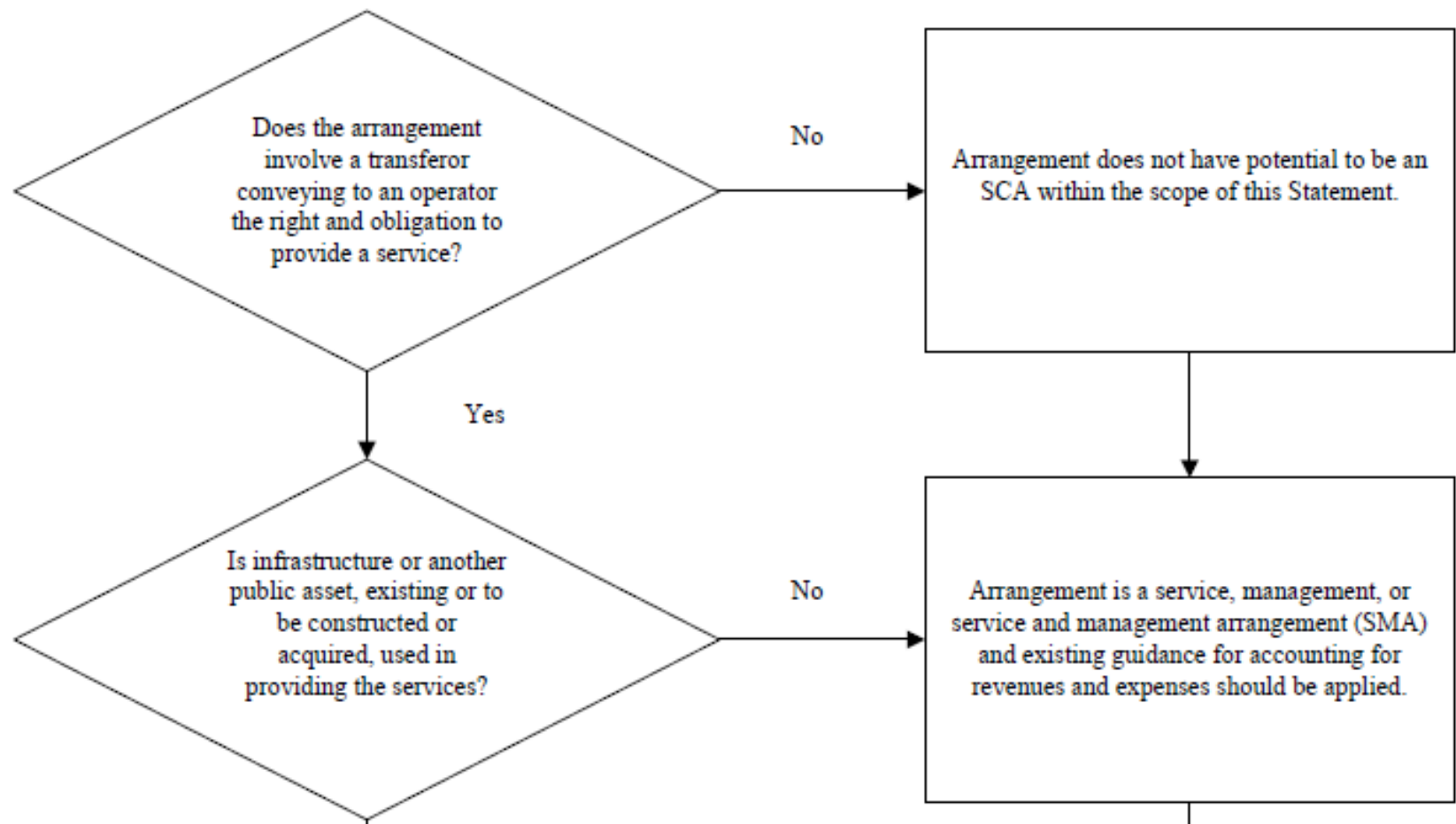


Note Disclosures

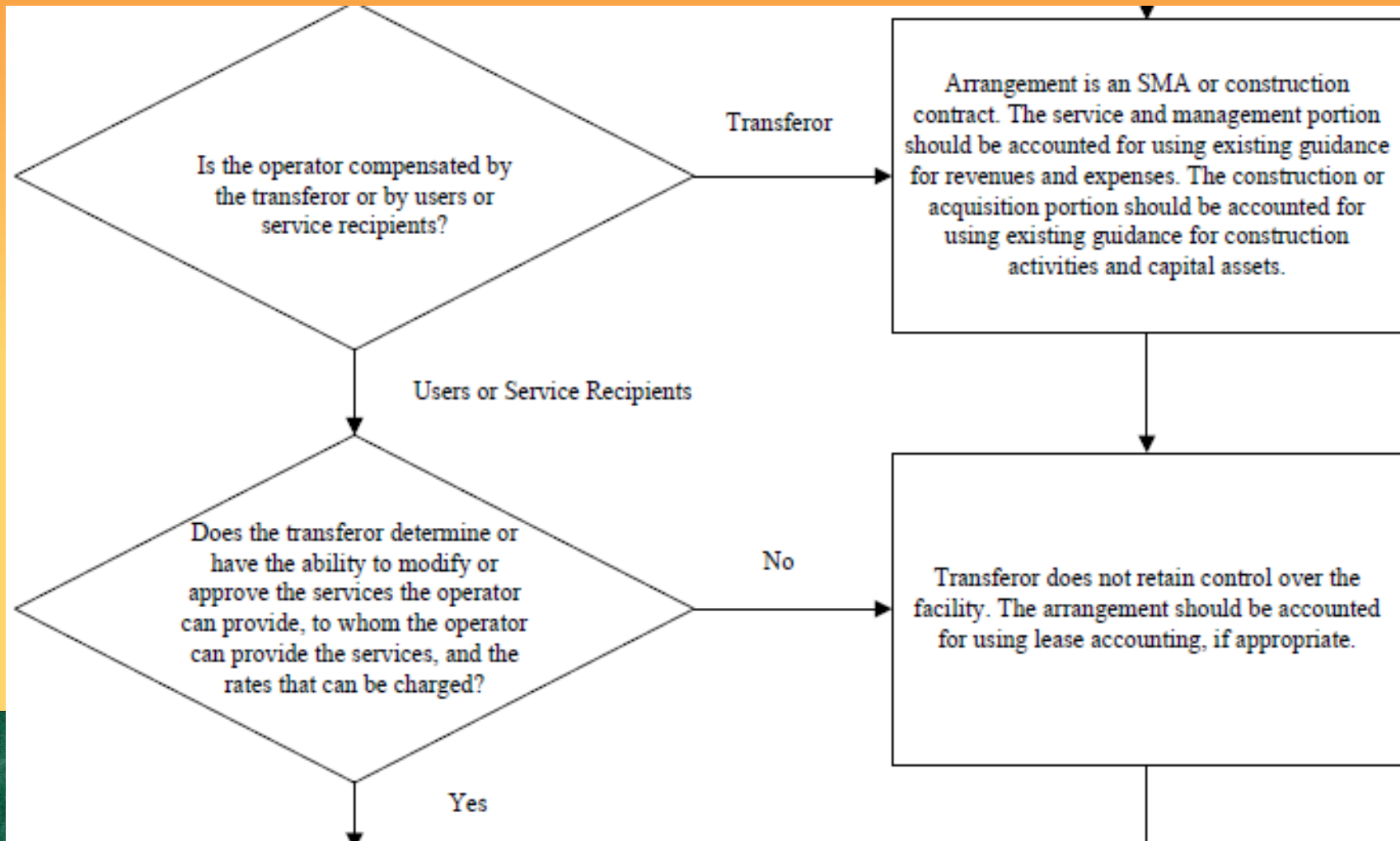
- The following information should be disclosed in the notes to the financial statements of both the transferor and government operator
 - A general description of the arrangement
 - Including management's objectives for entering into the arrangement
 - If applicable, the status of the project during the construction period
 - Nature and amounts of assets, liabilities, and deferred inflows of resources related to the SCA that are recognized in the financial statements
 - Nature and extent of rights retained by the transferor or granted to the government operator
 - If applicable, disclosures should be made about guarantees and commitments, including identification, duration, and significant contract terms of the guarantees or commitments.



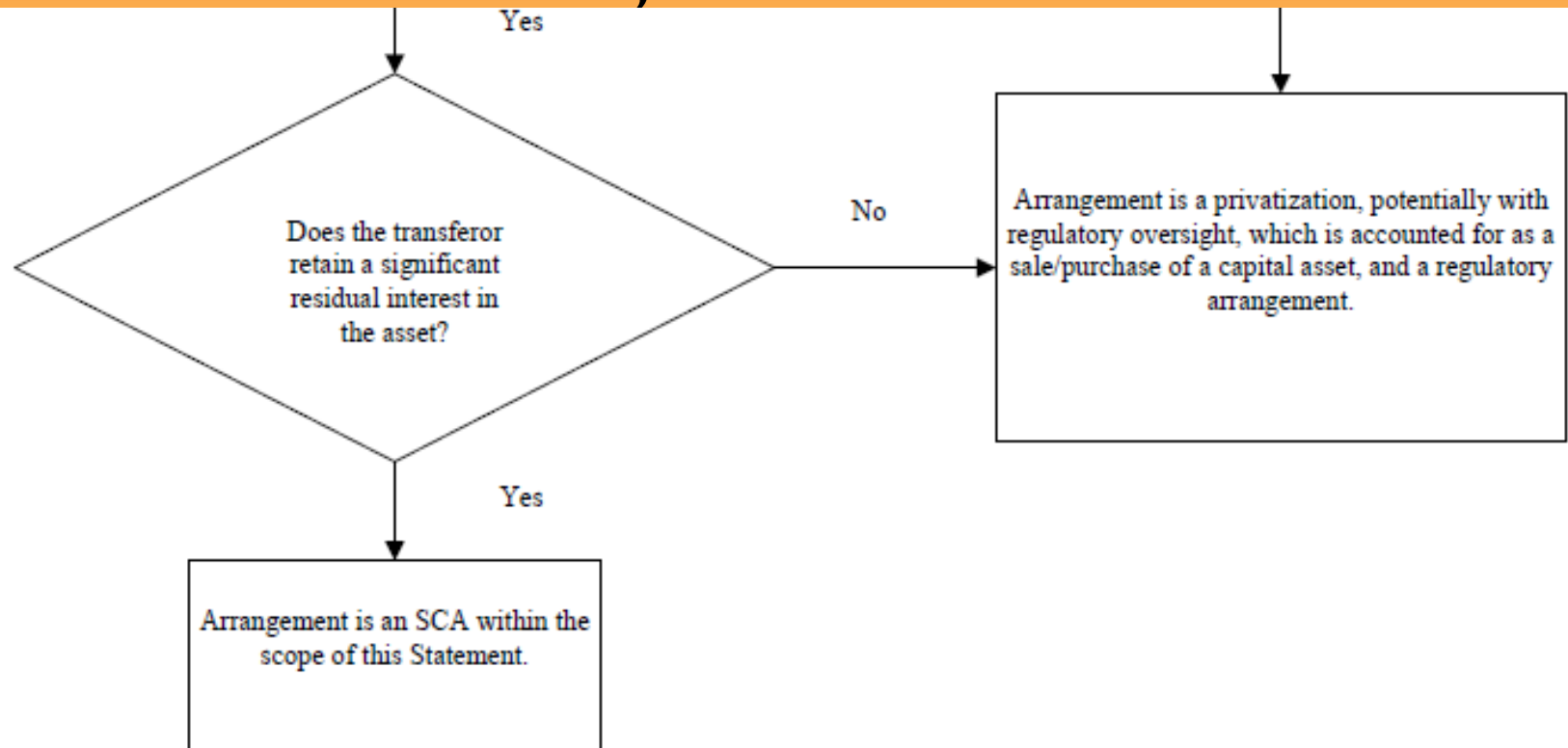
GASB 60- Service Concession Arrangements (SCAs) – a picture's worth 1,000 words



GASB 60- Service Concession Arrangements (SCAs) – a picture's worth 1,000 words

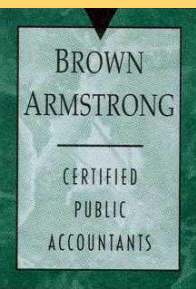


GASB 60- Service Concession Arrangements (SCAs) – a picture's worth 1,000 words



Practical Implementation Guidance

- Question should always be asked –
 - Is this a lease or a management contract?
 - Unless a capital lease, leases do not involve infrastructure or capital asset constructed or acquired to be used in providing services
 - Could be a management arrangement / contract
 - Capital leases are a form of financing of asset where ultimate ownership transfers at the end of the period
 - No compensation other than payments, no ability to control, approve usage and no residual back to the government



2012 Capital Assets of a Government

	Beginning Balance	Increases	Decreases	Ending Balance
Governmental activities:				
<i>Capital assets, not being depreciated</i>				
Land	\$ 138,485	\$ 5,516	\$ -	\$ 144,001
Construction in progress	195,698	65,124	(121,642)	139,180
Infrastructure	3,344,626	131,474	-	3,476,100
Rights-of-way	595,018	14,587	(188)	609,417
Total capital assets, not being depreciated	4,273,827	216,701	(121,830)	4,368,698
<i>Capital assets, being depreciated/amortized</i>				
Buildings	1,512,952	97,163	-	1,610,115
Improvements other than buildings	120,913	-	-	120,913
Furniture and equipment	371,993	13,290	(7,327)	377,956
Software costs	155,203	18,464	(208)	173,459
Total capital assets, being depreciated/amortized	2,161,061	128,917	(7,535)	2,282,443
<i>Less accumulated depreciation/amortization for:</i>				
Buildings	(430,890)	(38,159)	-	(469,049)
Improvements other than buildings	(69,536)	(4,478)	-	(74,014)
Furniture and equipment	(290,691)	(24,380)	6,860	(308,211)
Software costs	(146,285)	(3,258)	203	(149,340)
Total accumulated depreciation/amortization	(937,402)	(70,275)	7,063	(1,000,614)
Total capital assets, being depreciated/amortized, net	1,223,659	58,642	(472)	1,281,829
Governmental activities capital assets, net	\$ 5,497,486	\$ 275,343	\$ (122,302)	\$ 5,650,527
Business-type activities:				
<i>Capital assets, not being depreciated</i>				
Land	\$ 568	\$ -	\$ -	\$ 568
Construction in progress	8,525	82	-	8,607
Total capital assets, not being depreciated	9,093	82	-	9,175
<i>Capital assets, being depreciated</i>				
Buildings	3,389	-	-	3,389
Improvements other than buildings	631	-	-	631
Furniture and equipment	5,614	280	(7)	5,887
Total capital assets, being depreciated	9,634	280	(7)	9,907
<i>Less accumulated depreciation for:</i>				
Buildings	(2,518)	(103)	-	(2,621)
Improvements other than buildings	(569)	(2)	-	(571)
Furniture and equipment	(4,875)	(301)	7	(5,169)
Total accumulated depreciation	(7,962)	(406)	7	(8,361)
Total capital assets, being depreciated, net	1,672	(126)	-	1,546
Business-type activities capital assets, net	\$ 10,765	\$ (44)	\$ -	\$ 10,721

2012 Capital Assets of a Government

Business Types

Capital assets, not being depreciated

	Beginning Balance	Increases	Decreases	Ending Balance
Construction in progress	\$ 75,776	\$ 40,211	\$ (89,078)	\$ 26,909
Land	82,627	-	-	82,627
Intangibles	808	-	-	808
Collections	11,304	320	(309)	11,315
Total capital assets, not being depreciated	170,515	40,531	(89,387)	121,659

Capital assets, being depreciated

Buildings	2,241,786	105,147	(25,818)	2,321,115
Land and improvements	112,728	1,254	-	113,982
Machinery and equipment	324,583	24,498	(15,277)	333,804
Intangibles	36,839	2,748	-	39,587
Library books and media	121,369	3,336	(4,831)	119,874
Total capital assets, being depreciated	2,837,305	136,983	(45,926)	2,928,362

Less accumulated depreciation for:

Buildings	(599,436)	(56,757)	8,260	(647,933)
Land and improvements	(81,760)	(3,944)	-	(85,704)
Machinery and equipment	(223,362)	(25,900)	13,842	(235,420)
Intangibles	(7,254)	(4,022)	-	(11,276)
Library books and media	(109,894)	(5,066)	4,536	(110,424)
Total accumulated depreciation	(1,021,706)	(95,689)	26,638	(1,090,757)
Total capital assets, being depreciated, net	1,815,599	41,294	(19,288)	1,837,605

Business Types,
net

\$ 1,986,114	\$ 81,825	\$ (108,675)	\$ 1,959,264
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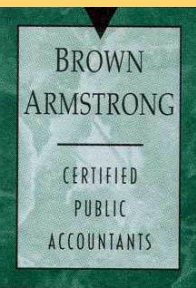
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Exercise (wagering is OK)

The Legislative body passes a bill that is signed by the Chief Executive to enter into an arrangement with HFP Corp, a private operator based in Georgia for 2 of the dorm complexes in the University system (a business type activity). Two separate agreements are made:

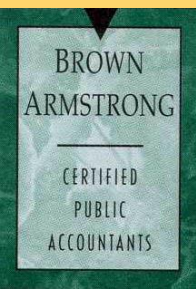
1. HFP will handle the operations, security and maintenance, etc. but not the food concessions for a period of twelve years starting on July 1, 2013.
2. HFP will add 20% additional capacity to the two dormitory complexes in the form of new construction to be completed by June 30, 2015. The housing space will be built on existing land of the University and the project will be overseen by the Board of Regents. At June 30, 2025, the University has the ability to renew the contracts for up to a period of an additional 28 years (to June 30, 2053) and can ask HFP to add additional capacity if needed. No later than June 30, 2053, the Dorms will return to the University in as good or better condition than when constructed.



Exercise (wagering is OK)

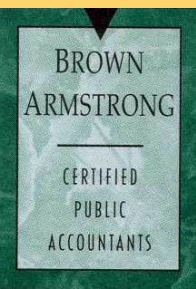
The 2 housing had an original construction cost of \$400,000,000. They are 50% depreciated and as of June 30, 2013, they have a net book value of \$200,000,000. The new capacity will cost \$100,000,000.

50% of each unit's rental charges that use the particular housing for the period from July 1, 2015 to June 30, 2025 will be retained by HFP. The housing department retains the remaining 50%. The present value of the payments to the department is estimated to be \$15 million as of July 1, 2013. Potential liabilities related to the arrangement are assumed by the University System. Approval of who is a Student remains with the University System.



Questions – take 10 minutes

- Does this qualify as an SCA?
- What are the debits and credits to be entered by the University System for
 - Initial construction
 - Depreciation
 - How about the collections of receipts?



Governmental Accounting Standards Series

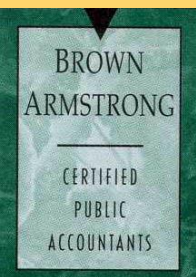
Statement No. 61
of the Governmental
Accounting Standards Board

The Financial Reporting Entity: Omnibus
an amendment of GASB Statements No. 14 and No. 34



Governmental Accounting Standards Board
of the Financial Accounting Foundation

GASB 61



STATE of MONTANA

GASB 61 – Modification of GASB

14/39 Component Units – Key Points

- Modifies fiscal dependency criteria to add that there must be financial benefit / burden between the potential component unit and the government
 - Result – some component units may no longer be component units and vice versa
- Also modifies blending so that if an entity exists ostensibly to sell debt on behalf of a primary government will now be required to be blended
- Clarifies equity interests in joint ventures



GASB 61 – Modification of GASB 14/39 Component Units

- “Misleading to Exclude” doctrine clarified
 - Primary Government has the responsibility to determine if a component unit should be included even if the tests aren’t met
 - Included because misleading to exclude
 - Result could be that some related organizations may become component units based on primary government’s policies



GASB 61 – Modification of GASB 14/39 Component Units – Key Points

- Fiscal Dependency Changed
 - The primary government is financially accountable if an organization is fiscally dependent on *and there is a potential for the organization to provide specific financial benefits to, or impose specific financial burdens on, the primary government regardless of whether the organization has (1) a separately elected governing board, (2) a governing board appointed by a higher level of government, or (3) a jointly appointed board.*



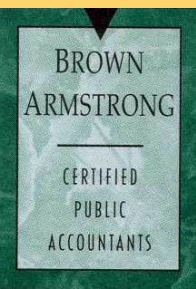
GASB 61 – Modification of GASB 14/39 Component Units – Key Points

- If a financial benefit or burden exists, then it is reported as part of the primary government's entity (discrete or blended)
- Specifically mentions school districts where a local general purpose government may approve the school board's budget or levy property taxes
 - They are component units to the local government if there is some form of approval
 - Could occur even if the City doesn't appoint the school board
 - Judgment allowed in most cases

GASB 61 – Modification of GASB

14/39 Component Units – Key Points

- “Major” Component Unit concept clarified
 - Include as major based on nature & significance to primary government – including:
 - Services provided to citizens
 - Significant transactions with primary government
 - Significant benefit / burden
 - Presentation can be
 - Columns on statement of net assets / activities
 - Combining after fund statements
 - Condensed financials in notes
 - Nonmajors aggregated – combining is OSI



GASB 61 – Modification of GASB 14/39 Component Units – Key Points

- Blending will now be required if
 - C/U's total debt outstanding, including leases, is expected to be repaid entirely or almost entirely with resources of the primary government
 - Usually a pledge exists
 - Result – end to “off balance sheet” financing

GASB 61 – Modification of GASB 14/39 Component Units – Key Points

- If government owns equity interest
 - Government's intent depends on reporting
 - Enhance providing of services – C/U
 - Rate of Return – Investment
- Transition
 - Now
 - Retroactive restatement



GASB-61 – Elimination of Profit in a Joint Venture Clarified

- Intent is to eliminate government transacting with itself in a JV
 - Participant's share of the net income on transactions with the joint venture would be treated as an additional equity interest in the joint venture rather than earnings from the joint venture
 - Total change in the equity interest in the joint venture would be unaffected, but the net increase in the equity interest would result from two factors rather than one.



GASB-61 – Elimination of Profit in a Joint Venture Clarified

- Example – A City has a 50% equity interest in an electricity-generating joint venture. (The equity interest is accounted for in an enterprise fund.)
 - Total sales were \$10,000,000.
 - Joint venture sales to City were \$3,000,000 (30% of total sales).
 - Net income was \$1,000,000 (10% of sales).
 - City's net equity interest in the joint venture increased by \$500,000 (50% of net income).



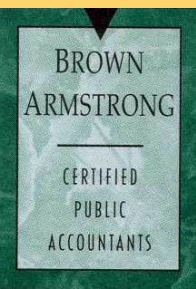
GASB-61 – Elimination of Profit in a Joint Venture Clarified

Example – Calculations

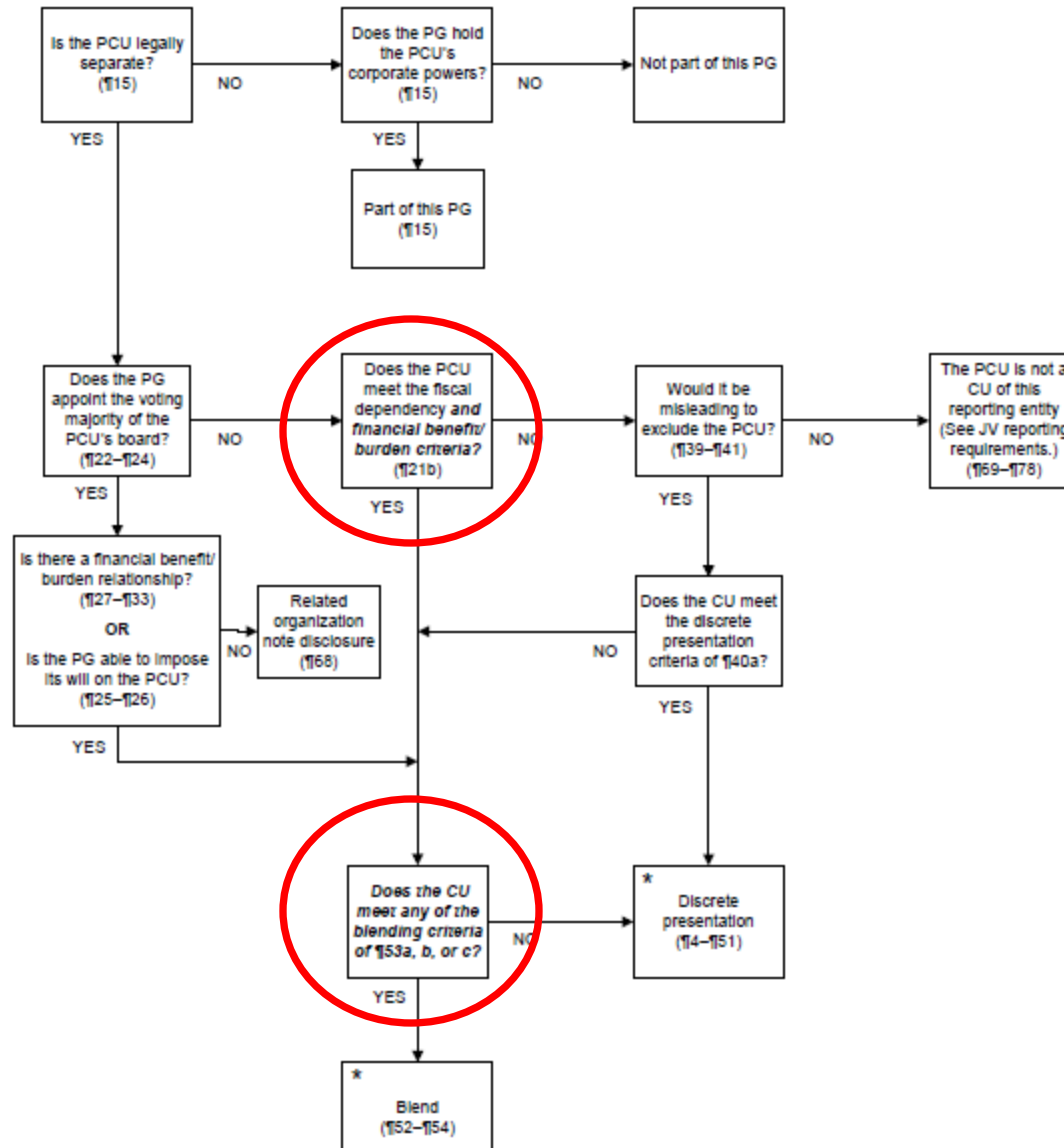
City's share of JV net income	\$500,000
Less: profit on intra-entity transactions ($\$300,000 \times 50\%$)	<u>(150,000)</u>
Net income from JV	\$350,000
Debits and Credits:	
DR. Investments	\$500,000
CR. Net income from JV	\$350,000
CR. Operating Expense – Utilities	\$150,000

Best Practices – Component Units

- Scan the Code, Laws, Ordinances etc. annually and look for key words in new laws
 - Commission
 - Authority
 - Board
 - System
 - Fund
- Document all “hits”
- Certify decision-making to auditor
- Document Controller judgment when using “misleading to exclude” paragraphs



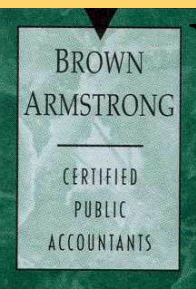
Italics = changes by GASB 61



GASB 61 –
Modification
of GASB 14/39
Component
Units– a
picture's worth
1,000 words

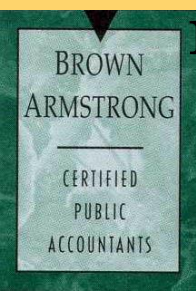
Key Questions on GASB-61

- What is financial accountability?
- An organization concludes that it qualifies as a component unit of a primary government based on the “misleading to exclude” criterion in paragraph 12 of Statement 14, as amended by GASB-61, but the primary government does not reach the same conclusion. Should the organization identify itself as a component unit of the primary government?



Key Questions on GASB-61

- In evaluating whether it would be misleading to exclude an organization from a reporting entity, pursuant to the provisions of paragraph 1 of Statement 14, as amended by GASB-61, should the method of display (blending or discrete presentation) be considered?
- Can a primary government include another primary government as a component unit on the basis that its financial statements would be misleading if the other primary government was not included in the reporting entity?



Key Questions on GASB-61

- What criteria should be used to determine which component units are “major”?
- What are the criteria for a component unit to be blended with the primary government?
- A component unit would be discretely presented under the provisions of Statement 14, as amended by GASB-61; however, in its day-to-day operations, the component unit does not act as a separate legal entity and operates in the same manner as departments or agencies of the primary government. Can the component unit be reported as part of the primary government or as a blended component unit?

Key Questions on GASB-61

- Are extensive note disclosures required for component units?
- Are individual component unit disclosures required for all discretely presented components?

GASB 62

NO. 309-C | DECEMBER 2010

Governmental Accounting Standards Series

Statement No. 62 of the
Governmental Accounting
Standards Board

Codification of Accounting and Financial
Reporting Guidance Contained in
Pre-November 30, 1989 FASB and
AICPA Pronouncements



GOVERNMENTAL ACCOUNTING STANDARDS BOARD
OF THE FINANCIAL ACCOUNTING FOUNDATION

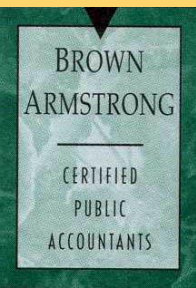
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GASB 62

- Why Was This Issued?
 - FASB Standards applied by governments all the time
 - Election in GASB-20, paragraph 6 used by BTAs
 - Old FASB Standards (e.g. FASB 116) don't exist anymore
 - AICPA standards sometimes in conflict with GASB standards
 - Clarity project of AICPA auditing standards removes direct references to GAAP
 - Removes “urban legends”
- No new GAAP – but items “left on the table”



GASB 62 – Which Bases of Accounting Apply What?

Both Governmental And Business Type OK – subject to reporting distinctions of Governmental Funds	Business Type Activities / Fund Types Only
Special and Extraordinary Items	Capitalization of Interest
Contingencies	Revenue Recognition with a Right of Return
Related Parties	Inventory
Leases	<p>Regulated Operations – as long as:</p> <ul style="list-style-type: none"> -Rates are established by independent regulator or by governing board with that power -Rates are designed to recover costs -Rates are assumed to be collectible

GASB 62 – Which Bases of Accounting Apply What?

Items That Apply to ALL Fund Types	
Revenue Recognition – Exchange Transactions	Troubled Debt Restructuring
Statement of Net Assets Classification	Foreign Currency Transactions
Comparative Financial Statements	Imputation of Interest
Prior Period Adjustments	Investment in Common Stock
Accounting Changes / Errors	Nonmonetary Transactions
Disclosure of Accounting Policies	Sales of Real Estate
Construction Contracts – Long Term	Research and Development Operations
Extinguishment of Debt	Broadcasters
Cable TV Operations	Lending Activities
Insurance Entities (not risk pools)	Mortgage Banking Activities

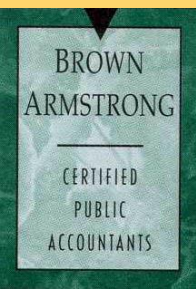
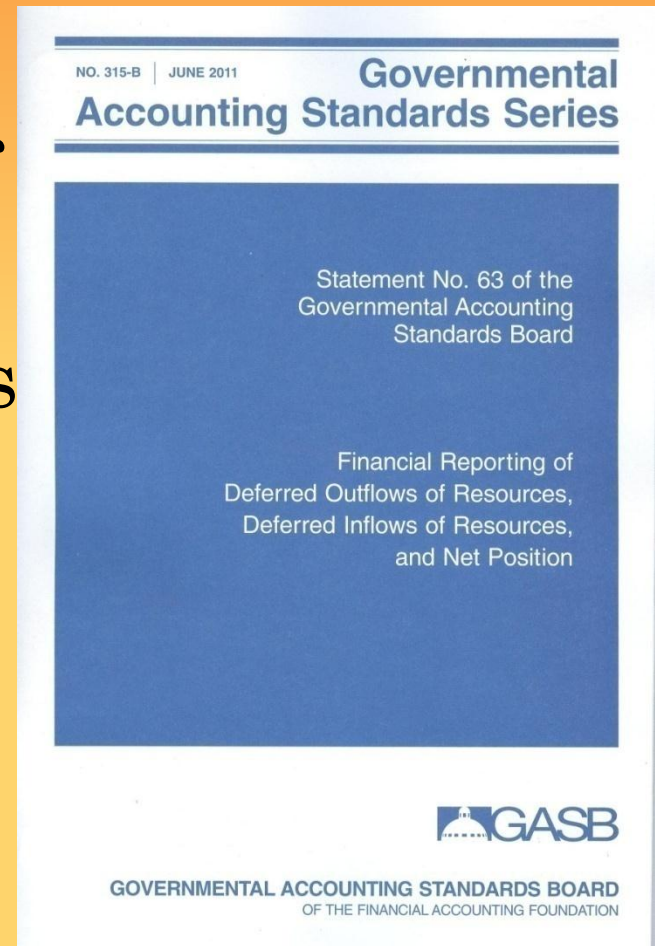
GASB 62 – Items in GASB 62 Slated for Reexamination in the Future

- Capitalization of Interest
- Real Estate (Rentals / Sales)
- Extinguishment of Debt
- Inventory
- Leases
- Nonmonetary Transactions
- Prior-Period Adjustments / Changes / Errors
- Regulated Operations
- Research and Development
- Revenue Recognition – Exchange Transactions
- Troubled Debt Restructuring



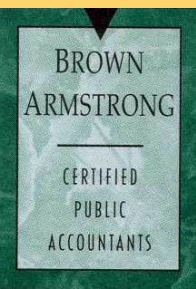
Statement No. 63

- Financial Reporting of Deferred Inflows of Resources, Deferred Outflows of Resources and Net Position



Background

- Concepts Statement 4 identifies 5 elements that make up a statement of financial position:
 - Assets
 - Liabilities
 - Deferred outflows of resources
 - Deferred inflows of resources
 - Net position
- This differs from the composition currently required by Statement 34, which requires the presentation of assets, liabilities, and net assets in a statement of financial position
- Statements 53 and 60 require deferrals
- Statement 65, 67, 68, 69 and 70 will require deferrals upon implementation



Definitions

- **Deferred outflows of resources**
 - A consumption of net assets by the government that is applicable to a future reporting period
 - Has a positive effect on net position, similar to assets
- **Deferred inflows of resources**
 - An acquisition of net assets by the government that is applicable to a future reporting period
 - Has a negative effect on net position, similar to liabilities

Definitions

- **Net position**
 - The residual of all elements presented in a statement of financial position



Accounting Equations

- Governmental activities in Government-wide statements:

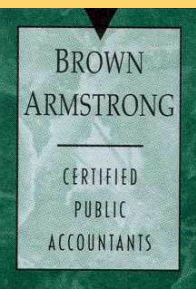
Statement of Net Position:

assets + deferred outflows – liabilities –
deferred inflows = net position

- Governmental fund format:

Balance sheet:

assets + deferred outflows = liabilities +
deferred inflows + fund balance



Provisions

- Deferred outflows should be reported in a separate section following assets, with a separate subtotal (but the two may be combined to provide a further subtotal)
- Deferred inflows should be reported in a separate section following liabilities, with a separate subtotal (but the two may be combined to provide a further subtotal)

Provisions

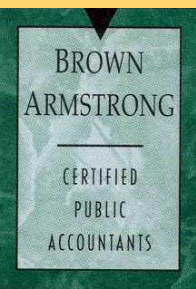
- Net Position components resemble net asset components under Statement 34, but include the effects of deferred outflows and deferred inflows
 - Net investment in capital assets
 - Restricted
 - Unrestricted

Net Investment in Capital Assets vs. Invested in Capital Assets Net of Related Debt

- ICANRD
 - Carrying value of capital assets LESS
 - Related debt LESS
 - *Significant* unspent debt proceeds and
 - Adjustments for
 - Premiums
 - Discounts
 - Deferred amounts on refundings
- NICA
 - CV of Capital Assets LESS
 - Related debt LESS
 - Adjustments for
 - Premiums
 - Discounts
 - Deferred amounts on refundings
 - **Related deferred inflows / outflows of resources unless attributable to unspent resources**

What About Unspent Bond Proceeds

- Principle - The *net investment in capital assets* component of net position consists of:
 - Capital assets, net of accumulated depreciation, *less*
 - Outstanding balances of
 - Bonds, mortgages, notes, or other borrowings that are attributable to the acquisition, construction, or improvement of those assets,
 - Deferred inflows /outflows and related debt.



What About Unspent Bond Proceeds

- Principle - If there are *significant* unspent related debt proceeds or deferred inflows of resources at the end of the reporting period, the portion of the debt or deferred inflows of resources attributable to the unspent amount **should not be included in the calculation of net investment in capital assets**. Instead, that portion of the debt or deferred inflows of resources should be included in the same net position component (**restricted** or unrestricted) as the unspent amount. **Why?**

Statement of Net Position

	Primary Government			Component Units
	Governmental Activities	Business-type Activities	Total	
ASSETS				
Cash and cash equivalents	\$ 11,712,829	\$ 10,516,820	\$ 22,229,649	\$ 303,935
Investments	29,250,291	64,575	29,314,866	7,428,952
Derivative instrument—rate swap	1,040,482		1,040,482	
Receivables (net)	11,792,650	3,609,615	15,402,265	4,042,290
Internal balances	313,768	(313,768)		—
Inventories	322,149	126,674	448,823	83,697
Equity interest in joint venture	2,303,256	—	2,303,256	—
Capital assets:				
Land, improvements, and construction in progress	28,435,025	6,408,150	34,843,175	751,239
Other capital assets, net of depreciation	141,587,735	146,513,065	288,100,800	36,993,547
Total capital assets	170,022,760	152,921,215	322,943,975	37,744,786
Total assets	226,758,185	166,925,131	393,683,316	49,603,660

DEFERRED OUTFLOWS

Accumulated decrease in fair value of hedging derivatives	—	127,520	127,520	—
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LIABILITIES

Accounts payable and accrued expenses	7,538,543	659,592	8,198,135	1,803,332
Advances from grantors	1,435,599		1,435,599	38,911
Forward contract		127,520	127,520	
Long-term liabilities:				
Due within one year	9,236,000	4,426,286	13,662,286	1,426,639
Due in more than one year	83,302,378	74,482,273	157,784,651	27,106,151
Total liabilities	101,512,520	79,695,671	181,208,191	30,375,033

DEFERRED INFLOWS

Accumulated increase in fair value of hedging derivatives	1,040,482	—	1,040,482	—
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NET POSITION

Net investment in capital assets	103,711,386	79,088,574	182,799,960	15,906,392
Amounts Restricted for:				
Transportation and public works	10,655,737	—	10,655,737	—
Debt service	3,076,829	1,451,996	4,528,825	—
Housing and community redevelopment	6,845,629	—	6,845,629	—
Other purposes	1,483,387	—	1,483,387	492,445
Unrestricted Amounts (deficit)	(1,567,785)	6,816,410	5,248,625	2,829,790
Total net position	\$ 124,205,183	\$ 87,356,980	\$211,562,163	\$ 19,228,627

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BROWN
ARMSTRONG

CERTIFIED
PUBLIC
ACCOUNTANTS

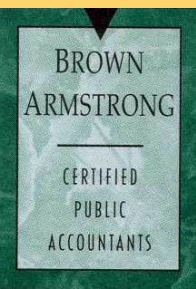
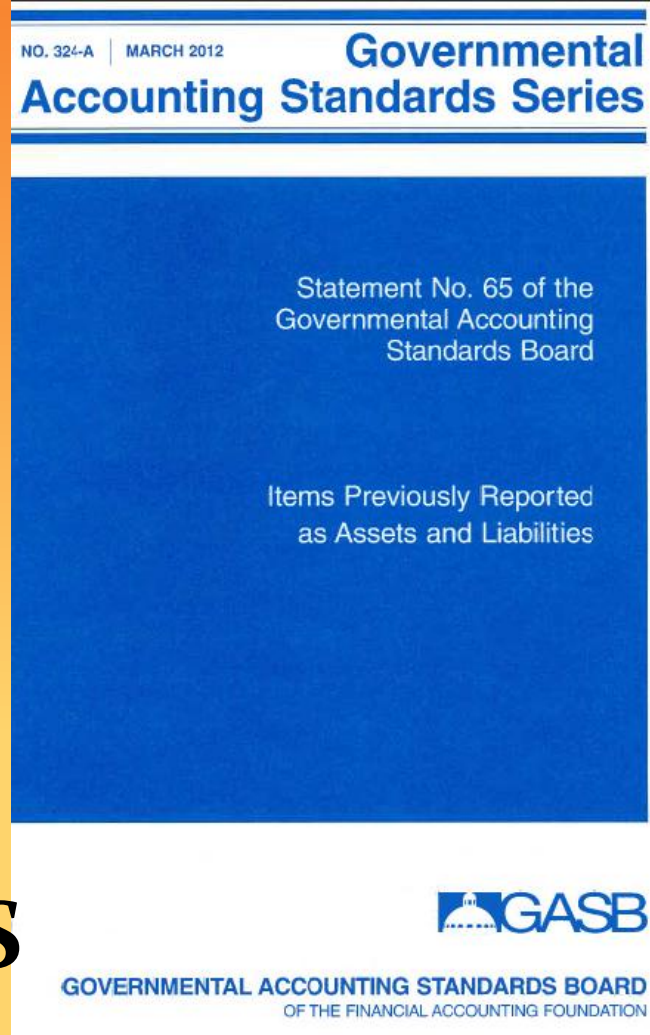
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Disclosures

- Governments should provide details of different types of deferred amounts in the notes if significant components of the total deferred amounts are obscured by aggregation on the face of the statements
- If the amount reported for a component of net position is significantly affected by deferred inflows or outflows, governments should disclose an explanation in the notes

Statement No. 65

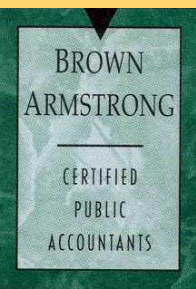
ITEMS PREVIOUSLY REPORTED AS ASSETS AND LIABILITIES



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Objective

- Examine the classification of certain items previously reported as assets or liabilities to determine whether any of these items should be reported as
 - A deferred outflow of resources or an outflow of resources (expense/expenditure), or
 - A deferred inflow of resources or an inflow of resources (revenue).
 - Paragraph 38 of Concepts Statement 4 **limits recognition of deferred outflows of resources and deferred inflows of resources to those instances identified by the GASB.**



Approach to Development of the Statement

- Hierarchy for applying the definitions of the elements in Concepts Statement 4.
 - Do items meet the definition of an asset or a liability?
 - If not, do they meet the definition of a deferred outflow of resources or a deferred inflow of resources?
 - If not, then the item should be recognized as an outflow of resources or an inflow of resources.



Continue to Report as an Asset

- Prepayments / Inventory (paragraph 73 of NCGA Statement 1)
- Resources **advanced** to another government in relation to a government-mandated nonexchange transaction or a voluntary nonexchange transaction *when **eligibility requirements** other than time requirements have not been met* (paragraph 19 of Statement 33)
- The purchase of future revenues from a government outside the financial reporting entity (paragraphs 13–16 of Statement 48)

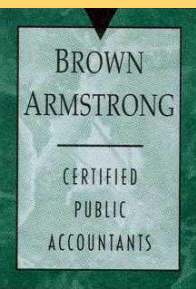


Continue to Report as an Asset

- Initial subscriber installation costs in relation to cable television systems (paragraph 398 of Statement 62)
- Capitalized incurred costs related to regulated activities (paragraph 480 of Statement 62)
 - Refunds of utility charges are liabilities (par. 482)
- Circumstances in which a pension plan's net position exceeds the total pension liability

Report as a Deferred Outflow

- Resources **advanced** to another government in relation to a government-mandated nonexchange transaction or a voluntary nonexchange transaction *when **time requirements** are the only eligibility requirements that have not been met* by the other government (paragraph 19 of Statement 33)
- Deferred debit amounts resulting from the refunding of debt (paragraph 5 of Statement 23)
- The purchase of future revenues *within* the same financial reporting entity (paragraphs 13–16 of Statement 48)



Report as an Outflow of Resources

- Acquisition costs for insurance entities and public entity risk pools (paragraphs 28–30 of Statement 10 and paragraphs 412–414 of Statement 62)
- Initial direct costs incurred by the lessor for operating leases (paragraph 227 of Statement 62)
- Debt issuance costs (paragraph 12 of Statement 7 and paragraph 187 of Statement 62)
- Net balance (debit) of direct loan origination costs, including any portion related to points, related to lending activities (paragraph 45 of Statement 10 and paragraph 434 of Statement 62) (Housing Finance Agencies / Lending)

Report as a Liability

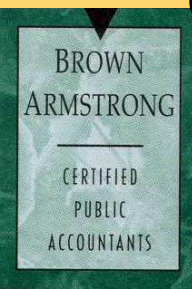
- Resources received in advance in relation to a derived tax revenue nonexchange transaction (paragraph 16 of Statement 33) (prepaid income, sales taxes, assessments)
- Resources **received** in advance in relation to a government-mandated nonexchange transaction (e.g. most programmatic grants) or a voluntary nonexchange (e.g. donations) transaction *when **eligibility requirements** other than time requirements have not been met* (paragraph 19 of Statement 33)
- Resources received in advance of an exchange transaction (paragraph 23 of Statement 62) (deposits)

Report as a Deferred Inflow

- Resources received in advance in relation to an *imposed* nonexchange transaction (paragraph 18 of Statement 33) (property taxes)
- Resources **received** in advance in relation to a government-mandated nonexchange transaction or a voluntary nonexchange transaction ***when time requirements are the only eligibility requirements that have not been met*** by the receiving government (paragraph 19 of Statement 33)
- Deferred credit amounts resulting from the refunding of debt (paragraph 5 of Statement 23, and paragraph 221 of Statement 62) (reacquisition price is > carrying amount of old bonds)

Report as a Deferred Inflow

- Proceeds from the sale of future revenues (paragraphs 13–16 of Statement 48).
- Unavailable revenue related to the application of modified accrual accounting (Statement 6 and Statement 33)
- Net balance (credit) of loan origination fees, excluding any portion related to points, for mortgage loans held for resale prior to the point of sale (paragraph 467 of Statement 62)



Revenue Recognition in Governmental Funds

- Revenues and other governmental fund financial resources should be recognized in the accounting period in which they become both measurable and available (NCGA Statement 1, paragraph 62).
- When an asset is recorded in governmental fund financial statements but the revenue is not available, the government should report a deferred inflow of resources until such time as the revenue becomes available.



Use of the Term *Deferred*

- Use of the term *deferred* should be limited to deferred outflows of resources and deferred inflows of resources
- Use of the term *unearned* was never allowable in Government GAAP except for certain insurance and risk pool revenues

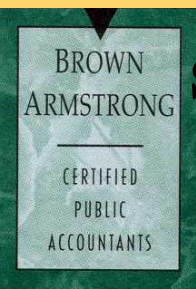
~~UNEARNED~~

~~DEFERRED~~

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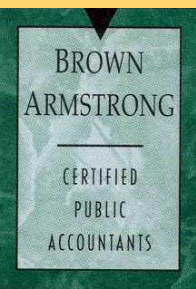
Key Questions on GASB-63 and 65

- GFOA likes the term “unearned revenue.” In fact, the Appendix D of the new GAAFR includes a line for Unearned Revenue on the Governmental Funds Balance Sheet and Statements of Net Position, however the GASB says the term "Unearned" will no longer be used. Why the discrepancy? What should it be called? (See next slide)



When to Use Unearned Revenue per GAAP

- For Profit
 - Publicly traded SEC registered companies where revenue has not been earned and needs to be credited to a nonmonetary liability account (FASB ASC-605-10-S99)
 - Airlines – tickets are sold but revenue not earned until a later date (FASB ASC 908-605-21)
 - Insurance – acquisition costs of policies, premiums in advance (FASB ASC 944 et seq)
 - Regulated industries – differences between net defined benefit period pension costs and allowable costs (FASB ASC 980-715-55)
- GASB
 - Public Entity Risk Pools – premium deficiency calculation factor in GASB-30 par. 4-5
 - Determines if revenue is sufficient to meet claims costs, claim adjustment expenses, and policyholder dividends expected to be incurred over the remainder of the policy term as well as expenses that are being deferred, such as acquisition costs.
 - No other reference
- **Which term to use to declare a liability for amounts of grants that need to be a liability per GASB-65?**



So What Is it?

- When should risk premiums generally be recognized as revenue by risk pools?
 - For example, Pool A assesses premiums based on the experience of the individual participating governments. The policy between each participant and Pool A is for one year. Because the policy period is one year, the revenue should be recognized by Pool A evenly over the year unless “the amount of risk protection changes according to a predetermined schedule.”
 - If Pool A's fiscal year is different from the policy year, the pool should report a liability in the statement of net position/balance sheet to the extent that the policy year extends beyond the fiscal year being presented.

What about Premium Deficiencies in Risk Pools?

- The purpose of the premium deficiency calculation is to determine if future revenues are sufficient to meet claims costs, claim adjustment expenses, and policyholder dividends expected to be incurred over the remainder of the policy term. The premium deficiency liability should be adjusted in future periods as expected costs become incurred costs so that no liability remains at the end of the period covered by the contracts. Although these deficiencies appear to relate only to future periods, they are the result of the pool's current-period underwriting efforts.
- Items to know to figure this out
 - Unearned premiums are now a liability
 - Claims costs
 - Claims expensed (function of IBNR)
 - Claims adjustments
 - Investment income
 - Dividends to pool participants



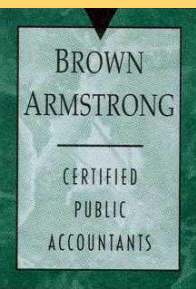
Major Fund Criteria

- Partial Restatement of GASB-34
- Assets should be combined with deferred outflows of resources and liabilities should be combined with deferred inflows of resources for purposes of determining which statements meet the criteria for major fund determination as set forth in paragraph 76 of Statement 34, as amended.



Other Q&As on GASB 65

- In a debt refunding, the difference between the reacquisition price and the net carrying amount of the old debt (refunded debt) should be reported as a deferred outflow of resources or as a deferred inflow of resources and recognized as a component of interest expense in a systematic and rational manner over the shorter of the remaining life of the old debt or the new debt (paragraph 4 of Statement 23). Does the remaining life of the old debt extend to its call date or its normal maturity date?
- When should resources received from tax audits be recognized?
- An entity levies amounts in its *current* property tax levy for *future* debt service payments. Should the amounts levied for the future-period debt service payments be reported as a deferred inflow of resources until those future periods start?

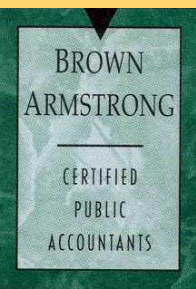


Key Questions on GASB-63 and 65

- If GASB 65 is *not* early implemented, then a section for Deferred Inflow or Outflow of Resources would only be reported if there are deferrals related to GASB 53 or GASB 60?
- If GASB 65 is *not* early implemented, then there will be no change to FY13 reporting of Deferred Revenue and Unearned Revenue (will be reported as liabilities)?

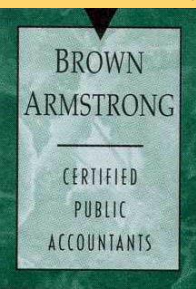
Key Questions on GASB-65

- A debt service agreement exists with a payment up front from a counterparty in exchange for debt service payments to be made according to a pre-determined schedule (in advance of the debt service payment due date, thus resulting in a loss of interest earnings to the State and an increase in interest earnings to the investment provider; revenue (interest income) is being recognized by the State over term of agreement - how should the remaining unamortized amount be reported under GASB 65?
- Does GASB 65 affect how the change in fair value of investments will be reported?
- Currently Taxation has significant receipts that they claim are either 1) overpayments to be applied to future taxes or refunded, or 2) suspense items, for which they cannot yet determine which period the revenue belongs in - how are these credit balances to be reported under GASB 65? How are taxes paid in advance of the period covered by the tax assessment accounted for?



Key Questions on GASB-65

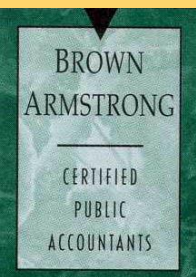
- A Gaming tax and a fee is imposed based on gross revenue for the preceding month, and the fee is an estimated payment for the third month following the month used as the basis of the gross revenue; therefore, June's collections are based on May's gross revenue and is payment for August; how are these advance payments reported under GASB 65?
- Should unspent Federal Grant revenues carried forward to next fiscal year be recorded as liabilities under GASB 65? Or could they be revenues?
- Federal grant reimbursements in the form of drug rebates are not received within the 60 day period after fiscal year end; Should this be considered "available" for revenue recognition purposes?
- How should a government record Federal Grant receipts from a 7 year grant award?



Armed with New Knowledge - Recasting a Statement of Net Assets

- Let's convert a Housing Division Together

Assets	
Cash with Treasurer	\$755,863
Cash with other officials	5,499.192
Investments	94,028,391
Mortgages Receivable	12,619,054
Accrued interest / dividends	7,488,628
Due from other funds	47,414
Prepaid expenses	103,291
Restricted investments	97,354,652
Current Assets	\$217,896,495

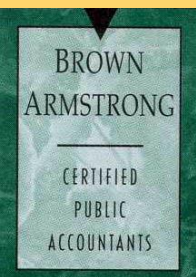


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Armed with New Knowledge - Recasting a Statement of Net Assets

- Let's convert a Housing Division Together

Assets	
Long term investments	261,757,357
Long term portion of mortgages	547,227,714
Notes / loans	108,450
Deferred charges	2,428,468
Restricted investments	6,006,196
Other	61,709
Long Term Assets	817,595,894
Total Assets	\$1,035,492,379

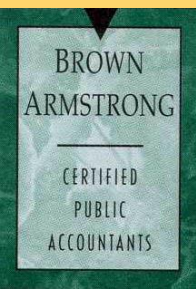


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Armed with New Knowledge – Recasting a Statement of Net Assets

- Let's convert a Housing Division Together

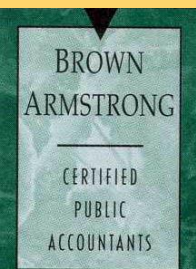
Liabilities	
Accounts payable	8,076,334
Accrued payroll	93,070
Interest payable	6,173,663
Due to other funds	3,137
Compensated absences	144,111
Current – Bonds Payable	13,630,000



Armed with New Knowledge - Recasting a Statement of Net Assets

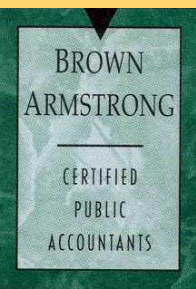
- Let's convert a Housing Division Together

Liabilities	
Compensated absences – LT	148,295
LT – Bonds Payable	797,375,612
EQUITY	
Restricted - Security of outstanding obligations	190,584,941
Restricted – regulation of business	6,143,430
Unrestricted	3,119,786
Net Assets	\$199,848,157



Questions

- What are the “low hanging fruit?”
- What likely will not be touched?
- P&L items include – what will likely change?
 - Interest income
 - Federal revenues
 - Other
 - Salaries and benefits
 - Operating charges
 - Interest on bonds
 - Servicers’ fees
 - **Bond issuance costs amortization – let’s discuss this one – guess what – you may have a restatement!**
 - Federal grant revenues – nonoperating
 - Federal grant expense – nonoperating
 - Transfers



**PENSION ACCOUNTING AND
FINANCIAL REPORTING BY
EMPLOYERS AND PLANS - GASB
67 AND GASB 68 *INCLUDING THE
SOON TO BE RELEASED TECHNICAL
CORRECTION TO GASB 68***

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GASB 67 and 68 Represent Huge Changes

- New standards approved June 25, 2012
 - Statement 67 replaces Statement 25 for Plan reporting
 - Statement 68 replaces Statement 27 for Employer reporting
- Major Game Changers in the new rules
 - ❶ Placing the Net Pension Liability on the Balance Sheet
 - ❷ Decoupling Expense from Funding
 - ❸ Accounting for Cost-Sharing Plans
 - ❹ Expanding Disclosure Information (Notes & RSI)
- Timing and Frequency, Effective Dates



Key Elements of 67 and 68

- Effective dates (later than was in Exposure Draft)
 - For plan reporting: Effective for all plans for plan years beginning after June 15, 2013 (2013/2014 for fiscal year plans or 2014 for calendar year)
 - For employer reporting: Effective for fiscal years beginning after June 15, 2014 (2014/2015)
- GASB “Implementation Guide” will be essential –
 - Plans *No later than June 30, 2013*
 - Employers *No later than March 31, 2014*
- OPEB coming in 2014-2015 with similar provisions
 - Exposure draft tentatively by June 30, 2014,



GASB Objectives and Goals

Financial Reporting Focus

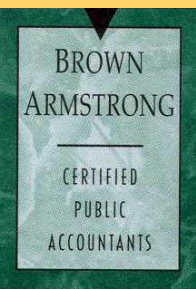
- GASB establishes accounting and financial reporting, not funding policies
- Focus on pension obligation, changes in obligation, and attribution of expense
- All determined consistent with GASB's "Concept Statements"

Long-Term Nature of Governments

- Cost of services to long-term operation
- "Interperiod equity" matches current period resources and costs

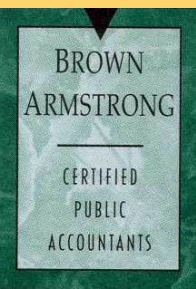
Employer-Employee Exchange

- Employer incurs an obligation to its employees for pension benefits
- Transaction is in context of a career-long relationship



Fundamental Approach

- Pensions viewed in the context of an ongoing, career-long employment relationship
- Focus on the cost to taxpayers over time of providing governmental services
- Accounting-based versus funding-based approach to measurement
- Defined pension benefits originate from exchanges between the employer and employees of salaries and benefits for employee services and are part of the total compensation for employee services



Scope: Criteria for Trusts

- Pensions provided through plans administered through trusts, or equivalent arrangements, in which:
 - Employer contributions (and related earnings) irrevocable
 - Plan assets dedicated to pensions
 - Plan assets legally protected from creditors

Implications: Criteria for Trusts

- Most pension trusts already meet all of the criteria
- Governments with pension benefits administered through trusts that *do not* meet all of the criteria would continue to apply GASB Statement 27 / 25
 - Therefore – 27 / 25 are AMENDED
- GASB expects to address pensions that do not meet the criteria in Phase 2 of the project

Liability Recognition

- The difference between the total pension obligation and plan assets held in trust for for pension benefits would be reported as a *net pension liability* in the financial statements of the employer government

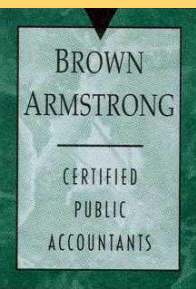
Measurement Steps

1. Projecting benefit payments based on terms of the plan and certain assumptions
2. Discounting the projected benefit payments to their actuarial present value
3. Attributing the present value of projected benefit payments to past and future years during which employees have worked or are expected to work.

Total Pension Liability (TPL):

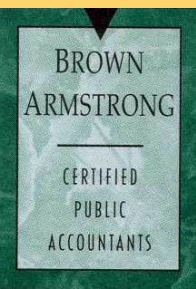
Timing and Frequency

- Measured as of a date no earlier than the employer's prior fiscal year-end (the measurement date)
- Actuarial valuation at least biennially
- Measurement of TPL can be from:
 - Actuarial valuation as of the measurement date
 - Update - **procedures rolling-forward amounts from an actuarial valuation as of a date no more than 30 months **plus 1 day** prior to the measurement date**
- Must reflect significant changes up to the measurement date



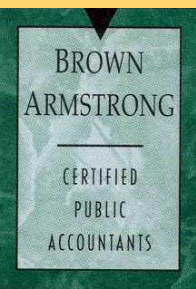
Big Deal #1 (the big one for auditors): Net Pension Liability Reported on Balance Sheet

- Net Pension Liability (NPL)
 - Total pension liability minus plan assets at market value (now “plan net position” as of June 16, 2012 due to GASB-63)
 - Similar to Unfunded Actuarial Accrued Liability (UAAL) but using market assets, not “smoothed” assets
- NPL must be reported on the employer’s balance sheet
 - Currently, UAAL is reported in the Required Supplementary Information (RSI)
 - Currently, only the Net Pension Obligation is reported on the balance sheet
 - Cumulative difference between annual required contribution (ARC) and actual contributions



Net Pension Liability Reported on Balance Sheet

- Total Pension Liability is an Actuarial Accrued Liability, calculated using:
 - Projected future benefits
 - Includes projected future service, salary increases and automatic Cost-of-Living Adjustments (COLAs)
 - Includes the cost of ad hoc COLAs if substantially automatic
 - A new “blended” discount rate
 - “Entry age” actuarial cost method
- NPL is then TPL minus market value of assets
 - Note asset smoothing still allowed (in determining pension expense), but reported separately
 - In Schedule of Deferred Inflows and Outflows of Resources



The New “Blended” Discount Rate

- Discount rate is based on projected benefits, current assets, and projected assets for current members
 - Projected assets **include future contributions** that fund benefits for current members
 - Projected assets do **not** include employer or employee contributions that fund service cost for future employees
 - For projected benefits that are covered by projected assets
 - Discount using long-term expected rate of return on assets
 - For projected benefits that are **not** covered by projected assets (i.e., after the “cross-over date”)
 - Discount using yield on 20-year AA/Aa tax-exempt municipal bond index
 - Solve for a single rate that gives the same total present value
 - Use that single equivalent rate to calculate the total pension liability (TPL)



Long-term Rate of Return Disclosures

- New note disclosures on the long-term rate of return
 - Description of how it was determined
 - Significant methods and assumptions used
 - Expected asset allocation
 - Real rates of return for each major asset class
 - Whether rates of return are arithmetic or geometric means
- Disclosures required regardless of whether or not they were actually used as direct inputs to determine the long-term rate of return



Big Deal #2 (the big one for actuaries and decisionmakers): Decoupling Expense from Funding

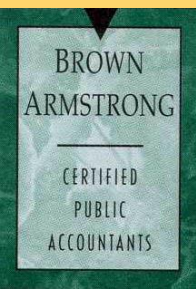
- Currently, pension expense is based explicitly on an actuarially determined funding requirement
 - The ARC, which is the “annual required contribution”
 - Even though is not required to be contributed!
 - Based on established practices for managing contribution volatility
 - Asset smoothing and UAAL amortization
 - The ARC served as a de facto funding standard
- New GASB pension expense is the change in NPL each year, with deferred recognition of only certain elements
 - Specifically **not** intended to be a funding target or standard



Big Deal #2 - Decoupling Pension Expense from Funding

- **Bulletin**

- Several organizations (NASRA, GFOA, AGA, NASACT, NLC, NCSL) are working on a white paper on pensions
 - Calling for best practice in continuing to provide an ARC
 - Funding in accordance with the ARC
 - Optimum ratio of plan net position to total pension liability



New Pension Expense Components

- Changes in Total Pension Liability that are recognized (i.e., expensed) immediately - no deferrals allowed
 - Service cost
 - Annual interest on the TPL
 - Projected investment returns over the year
 - All plan amendments
- Unchanged from Exposure Draft: Immediate recognition of all plan amendments, whether for all actives or retirees

New Pension Expense Components

- Changes in Total Pension Liability where some deferrals are allowed (i.e., expensed over multiple periods)
 - Changes in actuarial assumptions
 - Actuarial gains and losses
- These changes in TPL are recognized in expense over average expected remaining service lives of active and inactive members (including retirees)
 - Changed from Exposure Draft, where active and retired TPL changes were amortized separately
 - Simpler calculation than was in the ED, but similar impact on expense
 - Resulting amortization periods will still be very short

New Pension Expense Components

- Changes in Assets where some deferrals are allowed (i.e., expensed over multiple periods)
 - Differences between actual and projected earnings over the year (i.e., investment gain/loss)
 - Recognized in expense over closed 5-year period
 - Similar to current five-year asset smoothing
 - So the NPL on balance sheet will be “market volatile”, but effect on expense and on employer net position will still reflect smoothing
 - Through “Deferred Inflows and Outflows”
 - Effect on expense will be different from funding (and current ARC), where investment gain/loss is:
 - Smoothed over (typically) five years and
 - Also amortized as part of the UAAL



Big Deal #2 Decoupling Expense from Funding

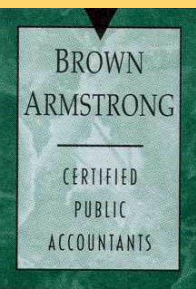
- The faster — *often immediate* — recognition of net pension liability changes will introduce much greater volatility in the reported pension expense.
 - This volatility will be reflected directly on the income statements of plan sponsors.
- This volatility is what disqualifies this new expense as a basis for determining a funding policy.
 - Means there will be two competing measures of plan cost
- Plans will want to review or adopt funding policies, now that GASB expense no longer provides funding guidance.
 - Funding policy also needed for discount rate — and for disclosures.



Big Deal #3 (the big one for statewide systems and Teachers Retirement Systems and Members):

Proportionate reporting for Cost-Sharing Plans

- Current standards have very simple reporting:
 - Pension expense is contractually required contribution
 - Balance sheet liability is the accumulated difference between the contractually required contribution and the actual contribution
 - No ARC or NPO (except as above)
 - Unfunded actuarial accrued liability is not reported at all
- New standards – treated like single employer plans:
 - Employers in “pooled” plans will now have that “pooled” liability and expense apportioned to each employer.
 - Recognize “proportionate share” of collective net pension liability, pension expense, and deferred inflows and outflows

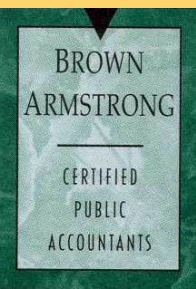


Cost-Sharing Plans

- Determining an employer's "proportionate share"
 - Basis should be consistent with the way required contributions are determined
 - "The use of the projected long-term contribution effort of the employer(s) ... is encouraged."
 - If "different contribution rates are assessed based on separate relationships that constitute the net pension liability ... the determination of the employer's net pension liability should ... reflect those separate relationships."
 - "For example, separate rates are calculated based on an internal allocation of liabilities and assets for different classes or tiers of employees"

Cost-Sharing Plans

- Measurement date
 - A cost sharing plan can determine its NPL (total pension liability and market assets) at one date each year
 - Probably the plan's valuation date
 - Each employer's share can be as of that same date
 - This is a welcome improvement over the ED
 - Still a substantial new burden for cost-sharing plans.



Example Schedule of Employer Allocations

EXAMPLE COST SHARING PENSION PLAN

Schedule of Employer Allocations

June 30, 2015

Final Design
might be 5 years
and average to
comply with
GAS-67

Employer/ Nonemployer (special funding situation)	2015 Actual Employer Contributions	Employer Allocation Percentage	
State of Example	\$ 2,143,842	38.9	%
Employer 1	268,425	4.9	
Employer 2	322,142	5.8	
Employer 3	483,255	8.8	
Employer 4	633,125	11.5	
Employer 5	144,288	2.6	
Employer 6	95,365	1.7	
Employer 7	94,238	1.7	
Employer 8	795,365	14.4	
Employer 9	267,468	4.9	
Employer 10	267,128	4.8	
Total	\$ 5,514,641	100.0	

Cost-Sharing Multiple-Employer Plans – Potential Solutions

- Include supplemental “schedule of plan pension amounts” in plan financial statements for which plan auditor engaged to provide opinion
 - Supplemental schedule of plan pension amounts include net pension liability, deferred outflows, deferred inflows, and pension expense for plan as a whole for which plan auditor is engaged to provide opinion
 - An alternative could be to include a “schedule of employer pension amounts”

Example Schedule of Employer Pension Amounts

EXAMPLE COST SHARING PENSION PLAN

Schedule of Pension Amounts

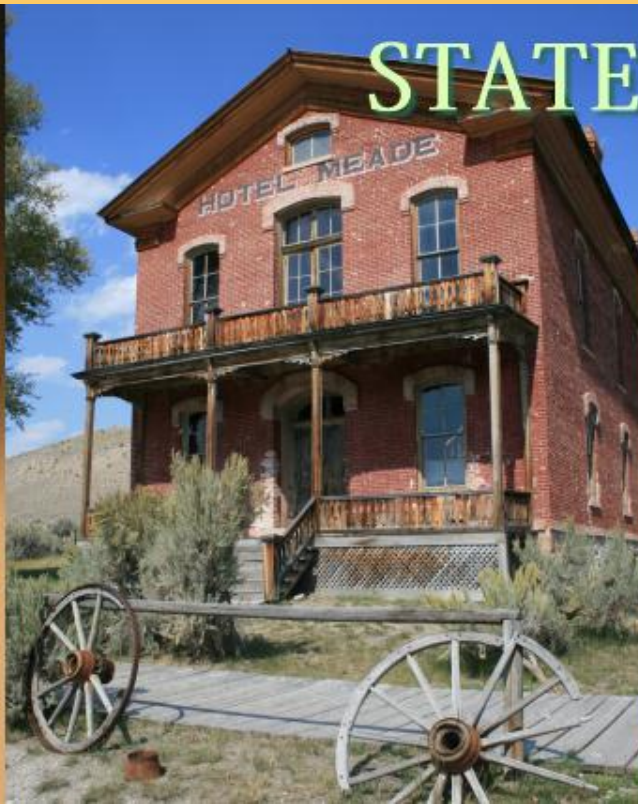
June 30, 2015

Employer/ Nonemployer (special funding situation)	Net Pension Liability	Deferred Outflow of Resources				Deferred Inflows of Resources				Pension Expense	
		Differences Between Expected and Actual Economic Experience	Differences Between Projected and Actual Investment Earnings	Changes of Assumptions	Changes in Employer Proportion and Differences Between Contributions and Proportionate Share of Pension Expense	Differences Between Expected and Actual Economic Experience	Differences Between Actual and Projected Investment Earnings	Changes of Assumptions	Changes in Employer Proportion and Differences Between Contributions and Proportionate Share of Pension Expense	Proportionate Share of Plan Pension Expense	Net Amortization of Deferred Amounts from Changes in Proportion and Proportionate Share of Pension Expense
State of Example	\$ 38,589,135	428,768	2,058,088	1,500,690	782,365	380,371	1,063,285	—	584,365	1,878,717	12,375
Employer 1	4,831,647	53,685	257,688	187,898	96,633	47,625	133,131	—	125,325	235,229	(1,793)
Employer 2	5,798,553	64,428	309,256	225,499	115,971	57,156	159,773	—	245,386	282,303	(8,088)
Employer 3	8,698,585	96,651	463,925	338,279	173,972	85,742	239,681	—	125,632	423,492	3,021
Employer 4	11,396,244	126,625	607,800	443,188	227,925	112,332	314,012	—	386,325	554,828	(9,900)
Employer 5	2,597,183	28,858	138,516	101,002	51,944	25,600	71,563	—	42,358	126,444	599
Employer 6	1,716,569	19,073	91,550	66,756	34,331	16,920	47,298	—	24,325	83,571	625
Employer 7	1,696,283	18,848	90,468	65,967	33,926	16,720	46,739	—	125,325	82,584	(5,712)
Employer 8	14,316,562	159,073	763,550	556,756	286,486	141,118	394,478	—	152,005	697,004	8,405
Employer 9	4,814,421	53,494	256,769	187,228	68,325	47,456	132,657	—	87,325	234,391	(1,188)
Employer 10	4,808,301	53,426	256,443	186,990	67,528	47,395	132,488	—	41,035	234,093	1,656
Total	\$ 99,263,485	1,102,928	5,294,055	3,860,249	1,939,406	978,435	2,735,105	—	1,939,406	4,832,655	—

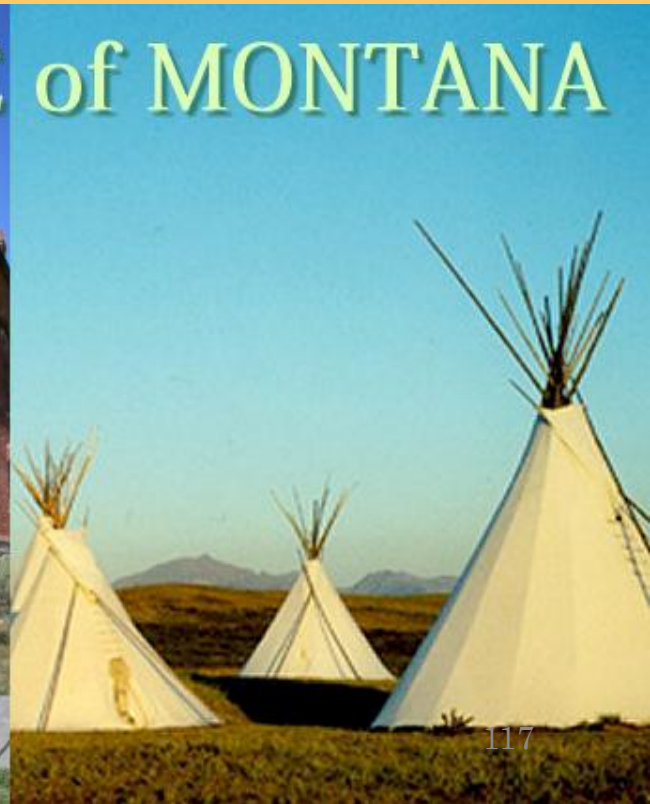
What About the Accounting and Audit Issues Related to Agent Multiple- Employer PERS?



BROWN
ARMSTRONG
—
CERTIFIED
PUBLIC
ACCOUNTANTS



STATE of MONTANA



Agent Multiple-Employer Plans – Issues

- Audited financial statements of the plan do not include actuarial information, nor do they include each employer’s “interest” in the fiduciary net position
- Allocation of fiduciary position reported by plan to employer is unaudited
- Employers needs the following elements to record as of the measurement date:
 - Total pension liability less fiduciary position = net pension liability
 - Deferred outflows/inflows based on investment experience
 - Deferred outflows/inflows based on changes in assumptions
 - Deferred outflows/inflows based actuarial gains and losses
 - Pension expense

How does a participating employer determine and get comfortable that these amounts as of the measurement date are accurate and verifiable?

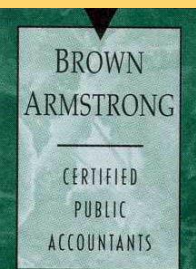
Potential Solution to Fiduciary Net Position

- Include supplemental condensed schedule of “changes in fiduciary position” by employer in plan financial statements for which plan auditor is engaged to provide opinion
- Plan auditor engaged to issue SOC 1 (type 2) report on allocation of inflows (i.e., contributions, investment income, etc.) and outflows (i.e., benefit payments, administrative expenses, etc.) of plan to individual employer accounts

Example Combining Schedule of Changes in Fiduciary Net Position (by employer)

Example Agent Multiple-Employer PERS
Combining Schedule of Changes in Fiduciary Net Position
Year ended June 30, 2015

	<u>Employer 1</u>	<u>Employer 2</u>	<u>Employer 3</u>	<u>Total</u>
Additions:				
Contributions:				
Employer	86,252,000	34,500,000	51,751,000	172,503,000
Member	32,662,000	13,065,000	19,597,000	65,324,000
Investment income:	80,965,000	20,347,000	37,112,000	138,424,000
Total additions	<u>199,879,000</u>	<u>67,912,000</u>	<u>108,460,000</u>	<u>376,251,000</u>
Deductions:				
Pension benefits, including refunds	384,635,000	184,352,000	228,356,000	797,343,000
Administrative expenses	4,716,000	1,886,000	2,829,000	9,431,000
Total deductions	<u>389,351,000</u>	<u>186,238,000</u>	<u>231,185,000</u>	<u>806,774,000</u>
Net increase (decrease)	(189,472,000)	(118,326,000)	(122,725,000)	(430,523,000)
Net position restricted for pension benefits:				
Beginning of year	5,843,645,000	1,468,538,000	2,678,595,000	9,990,778,000
End of year	<u>\$ 5,654,173,000</u>	<u>1,350,212,000</u>	<u>2,555,870,000</u>	<u>9,560,255,000</u>



Potential Solution to Total Pension Liability, Deferred Outflows/Inflows, and Pension Expense

- Plan auditor engaged to issue SOC 1 (type 2) report on census data controlled by plan (i.e. retired employees)
 - User controls at the plan level - Plan controls most of the information needed by the actuary (inactives/retirees)
 - User controls at the employer level – Employer controls the active employee information
 - Another alternative would be to have an AUP performed by the Plan auditor to provide substantive evidence to cover the collection and transmission of retirees/inactives
- Plan actuary issues separate actuarial report for each participating employer which includes net pension liability, deferred outflows/inflows by type and year, pension expense, and discount rate calculation
 - Employer management and employer auditor rely on actuary as management specialist for total pension liability for individual employer
- Employer auditor tests census data of active employees and confirms actuarial information used by actuary
- Employer and employer auditor responsible for validating deferred outflows/inflows and pension expense related to individual employer
 - Deferred outflows/inflows resulting from current year can be recalculated from condensed statement of changes in fiduciary position (by employer) included as supplemental information in plan financial statements
 - Rely on actuarial report for deferred outflows/inflows related to actuarial experience



Agent Multiple-Employer Plans – Other Issues

- Differentiation of actuarial assumptions for each participating employer
- Involvement of employer in establishing actuarial assumptions
- Ability of auditors of employers to evaluate appropriateness of actuarial assumptions
- Communication of auditors with plan actuary
- Ability of plan actuary to provide actuarial report directly to each employer

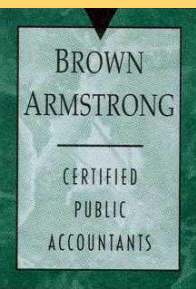
Special Funding Situations (Schools)

- A state or government that is not the employer contributes to the plan may be assuming a portion of the NPL
 - Example – Law governing a teacher retirement system requires the State to contribute 50% of the school district contributions on their behalf
- These “Nonemployer Contributing Entities” do not have to report a portion of the NPL on their balance sheets if:
 - The entity has no legal obligation to contribute or
 - The entity’s contribution requirement is defined in terms of a dedicated revenue stream
- Otherwise these entities must disclose their proportionate share of the collective NPL



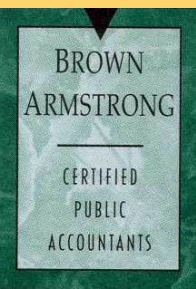
Expansion of Disclosure Information

- Includes both Notes and Required Supplementary Information (RSI)
- *Greatly* expanded plan and employer disclosures, including:
 - Description of the plan and assumptions
 - Policy for determining contributions
 - Sensitivity analysis of the impact on NPL of a one percentage point increase and decrease in the discount rate
 - Changes in the NPL for the past 10 years
 - Development of long-term earnings assumption
 - Annual rates of investment return for past 10 years (plan only)



Expansion of Disclosure Information

- More new disclosure information
 - “Actuarially determined employer contribution”
 - ADC is the “New ARC”
 - Basis and amount – if determined!
 - Comparison to amount actually contributed
 - May encourage review (or creation) of actuarial funding policy
- Expanded disclosures greatly increase the pension information needed for plan and employer’s financial statements.
 - New and challenging questions for employer’s financials:
 - Which actuary develops this information?
 - Who pays for it?



Comparison of Disclosure - Plans

	Single Employer Plan	Agent Multiple Employer	Cost Sharing Multiple Employer
Plan Description (Name, number of participating & nonparticipating employers, board description & composition, classes of members, authority for changes, contribution requirements)	Yes	Yes	Yes

Comparison of Disclosure - Plans

	Single Employer Plan	Agent Multiple Employer	Cost Sharing Multiple Employer
Plan Investments (Investment policies, description of fair valuing process, concentrations [>5% of plan position exc. US Governments], Annual Money-Weighted Rate of Return	Yes	Yes	Yes
Receivables	Yes	Yes	Yes

Comparison of Disclosure - Plans

	Single Employer Plan	Agent Multiple Employer	Cost Sharing Multiple Employer
Allocated Insurance Contracts	Yes	Yes	Yes
Reserves (descriptions, policy)	Yes	Yes	Yes
Deferred Retirement Option Plan (terms and balances)	Yes	Yes	Yes

Comparison of Disclosure - Plans

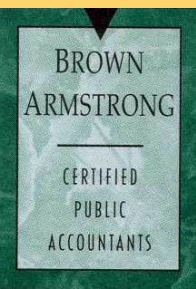
	Single Employer Plan	Agent Multiple Employer	Cost Sharing Multiple Employer
Components of Liability of Employers and Non-Employers (TPL, plan net position, NPL, Fiduciary net position)	Yes	NO	Yes
Significant Assumptions (COLAs, discount rate etc.)	Yes	NO	Yes
Actuarial valuation information	Yes	NO	Yes

Comparison of RSI - Plans

	Single Employer Plan	Agent Multiple Employer	Cost Sharing Multiple Employer
10 year change schedule of NPL	Yes	NO	Yes
10 year TPL, NPL, Covered Payroll	Yes	NO	Yes
IF ADC is determined, 10 year schedule comparing contributions to ADC	Yes	NO	Yes
Money Weighted Rate of Return	NO	Yes	NO

Updated Disclosure – EMPLOYERS

	Single Employer (example - Fire system)	Member of Agent Plan (Most PERSs)	Member of Cost Sharing Plan
Pension accounting elements (liabilities, assets, deferreds etc.)	Yes – component units reported separately	Yes – same as single employer	Yes – proportionate amounts
Pension Plan descriptive elements / sensitivity analysis	Yes – using “real rate of return”	Yes	Yes
Assumptions	Yes	Yes	Yes – how proportion is determined
Discount rate	Yes	Yes	Yes



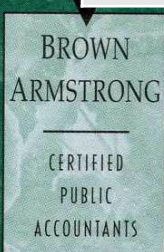
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Updated Disclosure – EMPLOYERS

	Single Employer (example - Fire system)	Member of Agent Plan (Most PERsSs)	Member of Cost Sharing Plan
Plan's fiduciary net position	Yes	Yes	Yes
Changes in NPL	Yes	Yes	NO
Valuation information	Yes	Yes	NO
If Special Funding Situation – proportion info – other items	Yes	Yes	Yes

RSI –EMPLOYERS

	Single Employer (example - Fire system)	Member of Agent Plan (Most PERSSs)	Member of Cost Sharing Plan
10 year schedule of NPL changes	Yes	Yes	NO
10 year schedule of pension liability, NPL, covered payroll etc.	Yes	Yes	If NO SFS then YES. IF SFS, then proportionate amount only
If ADC is done, comparison as of employer's FYE	Yes	Yes	NO
If NO ADC – contributions required and made	Yes	Yes	Yes



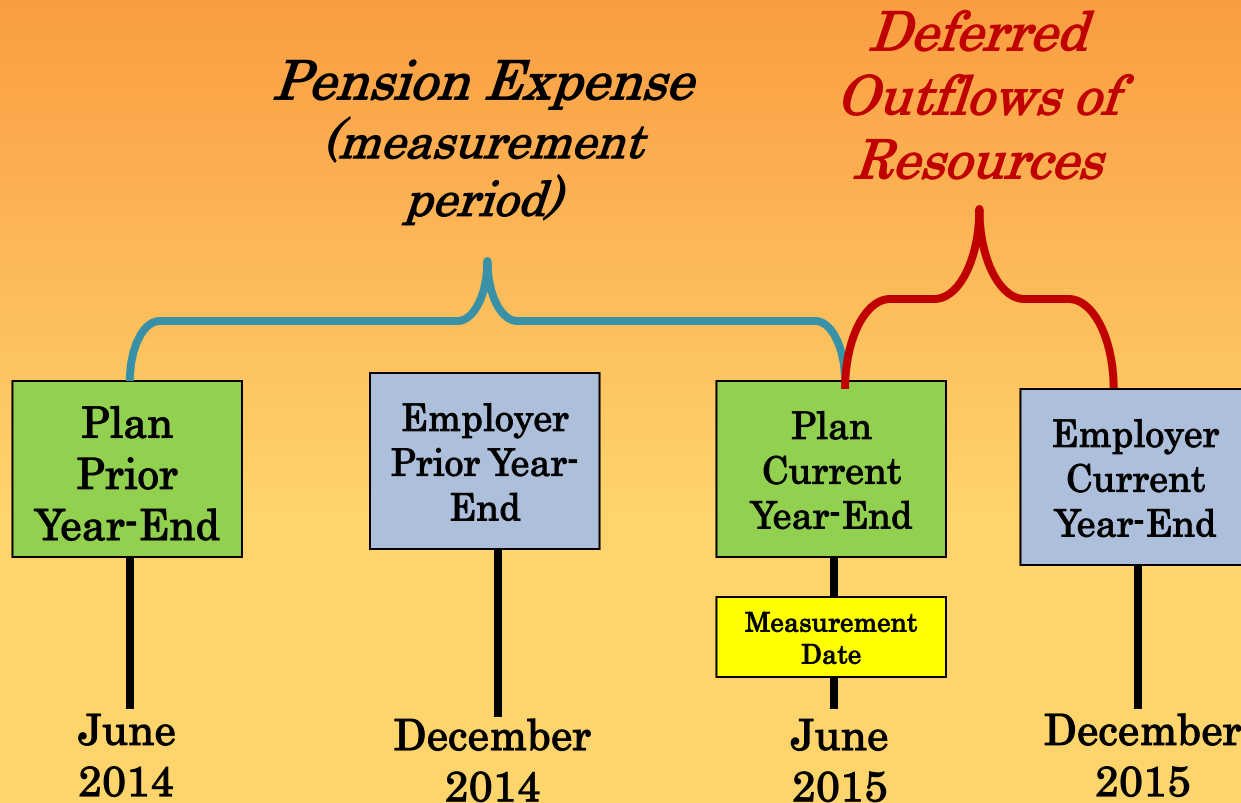
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Timing and Frequency of Measurement of Total Pension Liability

- Employers should report in their financial statements a net pension liability (asset) determined as of a *date (measurement date)* no earlier than the end of the employer's prior fiscal year for each defined-benefit pension plan in which they participate
- *The measurement date used should be consistently applied from period to period*
- Measurement of the total pension liability is determined through:
 - An actuarial valuation performed as of the *measurement date*, or
 - The use of update procedures to roll forward amounts from an actuarial valuation as of a date no more than *30 months and 1 day* earlier than the employer's year-end
 - Use professional judgment in determining extent of update procedures when changes in plan occur between last valuation date and the *measurement*

Measurement date will most likely correspond to year-end of plan. In this case, employers with same year-end as plan must choose measurement date as of their prior or current year-end.

Timing of Measurement of Total Pension Liability



Measurement date will most likely correspond to year-end of plan. Employer contributions made directly by the employer subsequent to the measurement date of the net pension liability and before the end of the employer's fiscal year should be recognized as a deferred outflow of resources.

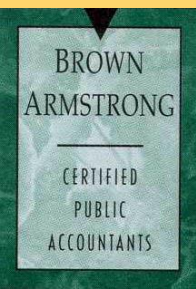
Example Sample City

Sample City participates in a cost-sharing multiple-employer defined-benefit plan sponsored by the State of Example.

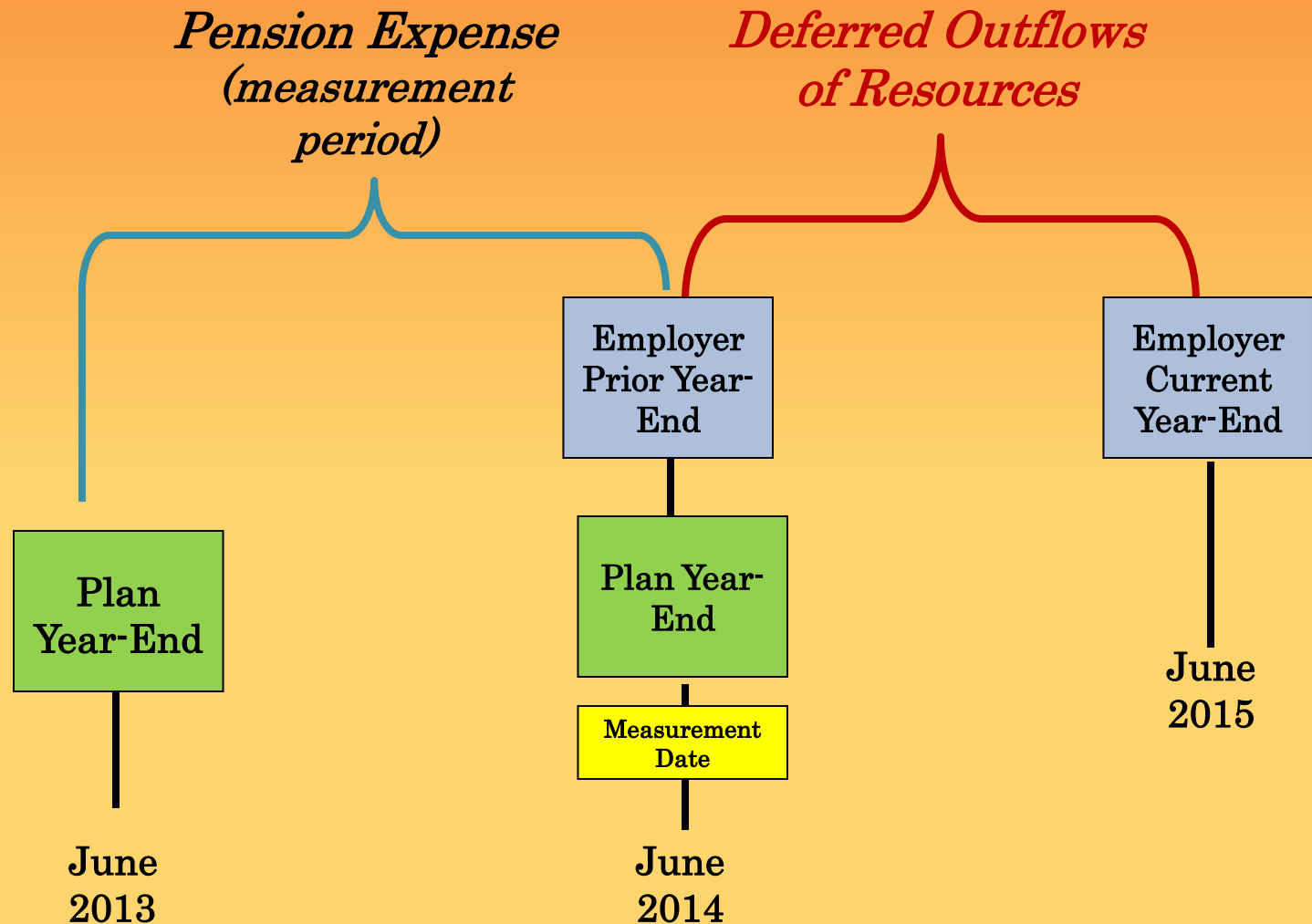
Sample City is implementing GASB Statement 68 during the year ended June 30, 2015. The cost-sharing plan also has a fiscal year-end of June 30th and implemented the provisions of GASB Statement 67 during the year ended June 30, 2014.

Sample City's financial statements are a single-year presentation.

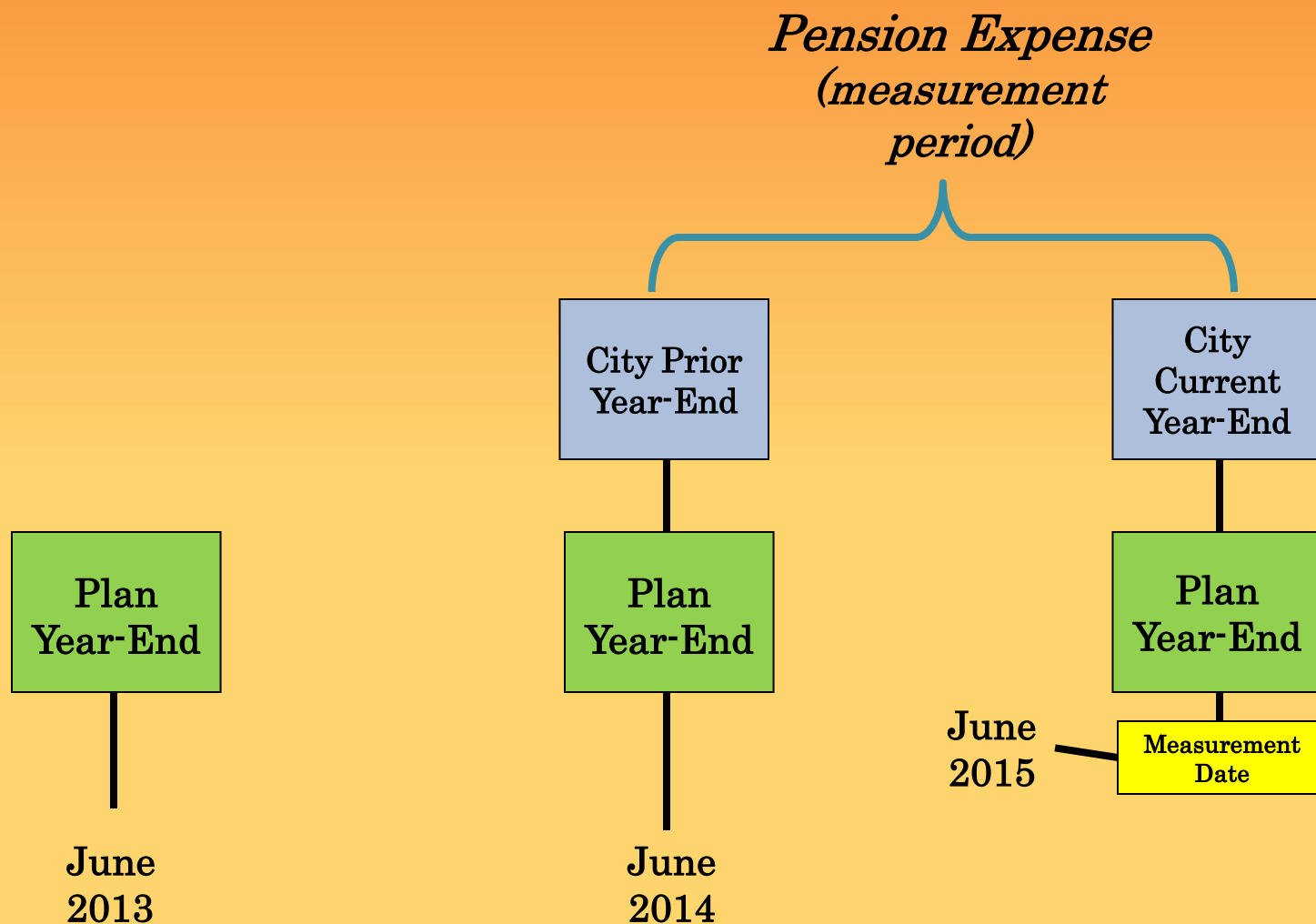
In accordance with GASB Statement 68, the measurement date for Sample City must be as of a date no earlier than the end of its prior fiscal year. Since Sample City and the Plan have the same year end, Sample City may elect to use June 30, 2014 or June 30, 2015 as the measurement date. However, once selected, the measurement date should be consistently applied from period to period.



Example Sample City – Impact of Using Prior Year Measurement Date



Example Sample City – Impact of Using Current Year Measurement Data



Another Way to Look at Timing of Valuation

Financial reporting period for year ended Dec. 31, 2012



AV date can be no earlier than June 30, 2010. If a date in the yellow zone is used, it must be updated to the measurement date.



Any date within this horizon is an appropriate measurement date.



If both the AV date and the measurement date are the same and are within this time period, a roll-forward is not required and dates are appropriate.

Bulletin – Technical Problem Uncovered in Implementing GASB-68 due to Deferrals

- GASB realized in April due to technical inquiries that employers will have a problem in implementing a provision of GASB-68 due to transition provisions of deferrals
 - Current provisions require if determination of *all* amounts of deferred inflows and outflows of resources is not practical at the beginning of the period of implementation, then deferred inflows / outflows of resources are not reported at the beginning of the period
 - See later slides on what gets expensed and what gets deferred / Amortized



Bulletin – Technical Problem Uncovered in Implementing GASB-68 due to Deferrals

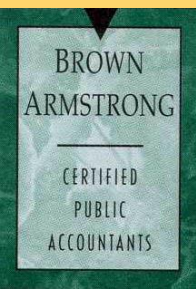
- GASB-68 also permits an employer to recognize a net pension liability measured as of a date one year prior to its fiscal year end
 - If used, from then forward, deferred outflows of resources recognized for contributions made subsequent to the measurement date but before the end of the employer's fiscal year
 - Realized as part of next valuation as prohibition of recognition as part of current pension expense until next measurement date



Bulletin – Technical Problem Uncovered in Implementing GASB-68 due to Deferrals

- **PROBLEM**

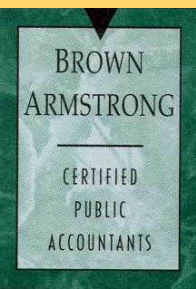
- If all deferred outflows of resources and deferred inflows of resources related to pensions cannot be determined as the beginning of the initial implementation period **significant underreporting of the restated net position could result even though the deferred outflows related to contributions are known**
 - Also results in a significant underreporting of pension expense in the first year of implementation



Bulletin – Technical Problem Uncovered in Implementing GASB-68 due to Deferrals

- PROBLEM

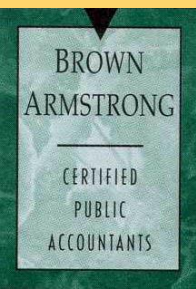
- Could also be a situation where employer made a contribution subsequent to the measurement date of the beginning net pension liability at transition but before the beginning of the initial implementation period. (2014-2015.)



Bulletin – Technical Problem Uncovered in Implementing GASB-68 due to Deferrals

- EXAMPLE

- Employer early implements for fiscal year ending June 30, 2014
- Beginning NPL determined as of June 30, 2012, (one year prior to the *beginning* of the fiscal year ending June 30, 2014)
- Contributions to the pension plan made between July 1, 2012, and June 30, 2013 would be recognized as a deferred outflow of resources at June 30, 2013.
- If *all* deferred outflows of resources and deferred inflows of resources related to pensions cannot be determined as of June 30, 2013, to comply with the requirement of GASB-68, the contribution-related amount **cannot be recognized as a beginning deferred outflow of resources at transition**

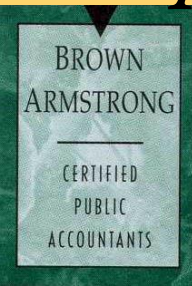


Bulletin – Technical Problem Uncovered in Implementing GASB-68 due to Deferrals

- **EXAMPLE**
 - Employer would have to adjust beginning net position for the impact of the amount of the contributions made between July 1, 2012, and June 30, 2013.
 - At June 30, 2014, the employer will have to account for the change in the net pension liability **during the reporting period**
 - Also includes the effect of the contributions made between July 1, 2012 and June 30, 2013.
- An exposure draft to address the problem is expected by June 2013.

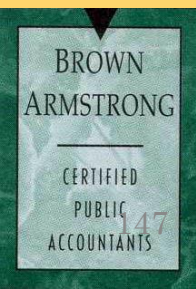


OTHER ASPECTS OF THE ACTUARIAL INFORMATION



Where to Start?

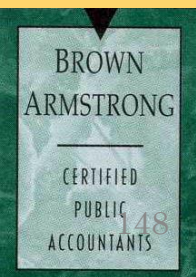
- Read statutes/plan document
 - Gain understanding of key provisions
- Obtain actuarial valuation report
 - Measurement date
 - Key assumptions
 - Plan provisions
- Obtain and test census data from actuary and payroll
- Obtain confirmation from actuary
- Evaluation of management's specialist
- We may consider the need for an auditor's specialist



Typical Actuarial Valuation Report

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Cover Letter	1
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Valuation Results:	
Sources and Uses of Funds	5
Contribution Rates	7
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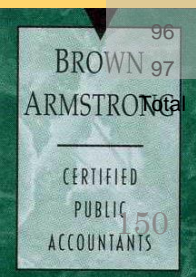
What the Auditor will be concerned with - Actuarial Assumptions

Investment Return Rate	→	7.25%
Wage Inflation Rate	→	4.0%
Pay increase Assumptions	→	4.0%
Assumed Retirement	→	62
Rates of: Mortality, Disability, Retirement, and Marriage	→	Actual Experience during 2008-2010 Period

The auditor must obtain an understanding of the actuarial methods and assumptions and assess their reasonableness and consistency of application.

Discount rate calculation

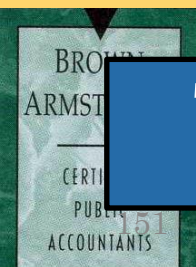
Year (a)	Projected Beginning Fiduciary Net Position (b)	Projected Benefit Payments (c)	Projected Benefit Payments		Actuarial Present Values of Projected Benefit Payments		
			"Funded" Portion of Benefit Payments (d)	"Unfunded" Portion of Benefit Payments (e)	Present Value of "Funded" Benefit Payments (f) = (d) ÷ (1 + 7.5%) ^(a)	Present Value of "Unfunded" Benefit Payments (g) = (e) ÷ (1 + 4%) ^(a)	Present Value of Benefit Payments Using the Single Discount Rate (h) = (c) ÷ (1 + 5.29%) ^(a)
1	\$ 1,431,956	\$ 109,951	\$ 109,951	\$ -	\$ 102,280	\$ -	\$ 104,427
2	1,500,197	116,500	116,500	-	100,811	-	105,088
3	1,565,686	123,749	123,749	-	99,613	-	106,019
4	1,628,547	131,690	131,690	-	98,610	-	107,154
5	1,687,890	140,229	140,229	-	97,678	-	108,370
6	1,742,722	149,168	149,168	-	96,655	-	109,487
7	1,792,194	158,466	158,466	-	95,516	-	110,468
8	1,835,463	168,332	168,332	-	94,384	-	111,450
9	1,871,402	178,591	178,591	-	93,150	-	112,302
10	1,898,930	189,069	189,069	-	91,925	-	112,918
26	547,880	322,779	322,779	-	102,135	-	84,503
27	316,985	326,326	-	-	-	-	81,140
28	64,800	328,997	-	-	-	-	77,694
29	-	330,678	-	-	-	-	74,168
30	-	331,266	-	-	-	-	70,567
96	-	1	-	1	-	-	-
97	-	-	-	-	-	-	-
Total				331,266	-	102,135	
					<div> <div>The sum of the present values of the two benefit payment streams is calculated.</div> </div>		
					<div> <div>\$ 2,109,333 + \$ 1,724,534 = \$ 3,833,867</div> </div>		



Census Data

- Key census data
 - Date of birth
 - Gender (male or female)
 - Date of hire or years of service
 - Date of termination or retirement
 - Marital status
 - Spouse date of birth
 - Eligible compensation
 - Employment status
- Auditing census data
 - Active employees
 - Inactive/retired
- Resolving exceptions

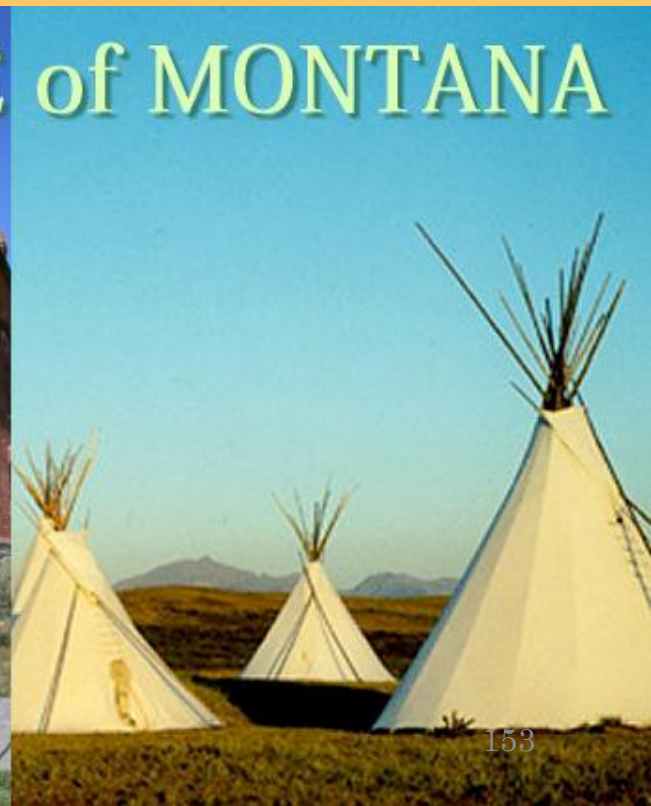
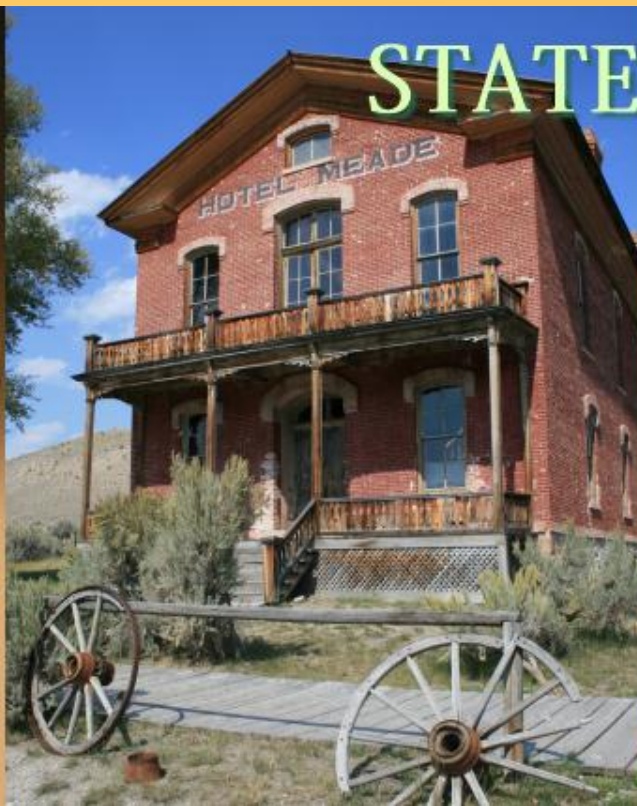
The auditor must test the reliability and completeness of the census data provided to the actuary



Census Data – Multiple-Employer PERS

- When auditing participant data in a multiemployer benefit plan, the auditor is often unable to directly test payroll records
- AICPA EBP Guide (§10.10) states census data for participating employers should be subject to testwork on a cycle basis – with a four year cycle being typical. Testing may be performed by:
 - In-house compliance personnel,
 - Employer auditors (i.e. agreed upon procedures), or
 - Auditor of plan

If Management Hires a Specialist and If We Hire a Specialist for Actuarial Information

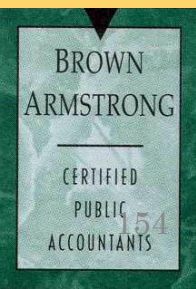


STATE of MONTANA

Specialists

Definitions

- Auditor's Specialist – Individual or organization possessing expertise in a field other than accounting or auditing, whose work in that field is used by the auditor to assist the auditor in obtaining sufficient appropriate audit evidence. An auditor's specialist may be either an auditor's internal specialist or an auditor's external specialist
- **Management's Specialist** – An individual or organization possessing expertise in a field other than accounting or auditing, whose work in that field is used by the entity to assist the entity in preparing the financial statements



Similarities Among and Differences Between Management and Auditor Specialists

Description	Management's specialists	Auditor internal specialists and resources	Specialists engaged by auditor
Specialists are a member of the engagement team	No	Yes	No - however, auditor directs their work
Auditor evaluates competence, capabilities and objectivity of specialists	Yes (AU-C-500.08(a), .A38-.A44)	Yes (AU-C-620.09, .A15-.A22)	Yes (AU-C-620.09, .A15-.A22)
Specialists may assist auditor in obtaining an understanding of the entity and its environment, including its internal control	No - however, they may provide relevant information	Yes (AU-C-620.A5)	Yes (AU-C-620.A5)

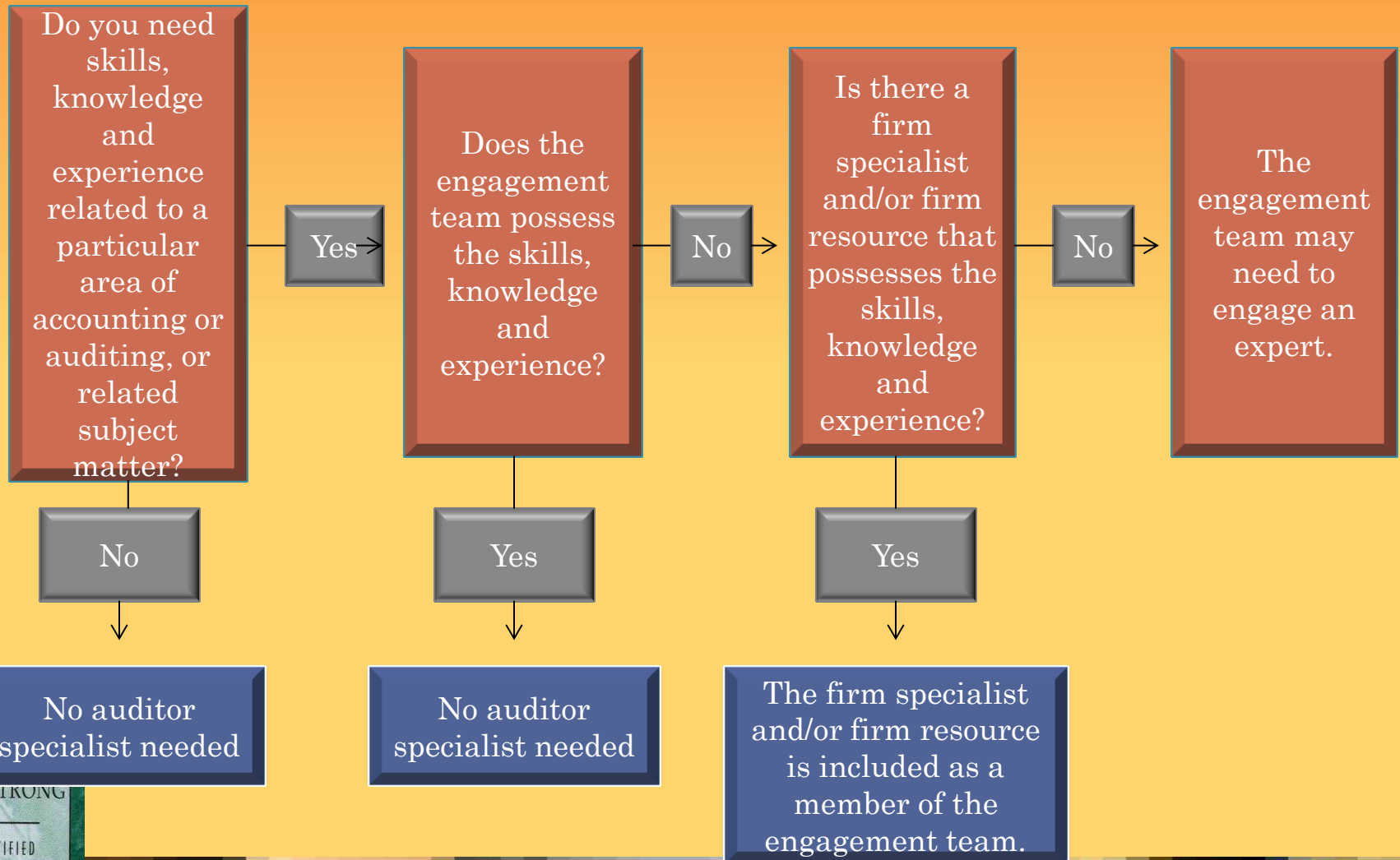
Similarities Among and Differences Between Management and Auditor Specialists

Description	Management's specialists	Auditor internal specialists and resources	Specialists engaged by auditor
Specialists may assist auditor in identifying and assessing risks of material misstatement	No - however, they may provide relevant information	Yes (AU-C-620.A5)	Yes (AU-C-620.A5)
Specialists may assist auditor in determining and implementing overall responses to financial statement level risks	No	Yes (AU-C-620.A5)	Yes (AU-C-620.A5)
Specialists may assist auditor in designing and performing further audit procedures to respond to the assessed risks at the assertion level, comprising test of controls or substantive procedures	No	Yes (AU-C-620.07 and .A5)	Yes (AU-C-620.07 and .A5)

Similarities Among and Differences Between Management and Auditor Specialists

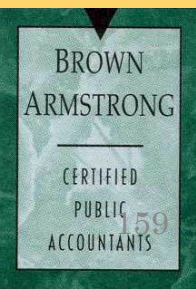
Description	Management's specialists	Auditor internal specialists and resources	Specialists engaged by auditor
Auditor obtains an understanding of the work of specialists	Yes (AU-C-500.08(b) and A.45-.A48)	Yes (AU-C-620.11 and .A25-A.29)	Yes (AU-C-620.11 and .A25-A.29)
Auditor evaluates the adequacy of the work of specialists	Yes (AU-C-500.08(c) and .A49)	Yes (AU-C-620.12 and .A35-.A42)	Yes (AU-C-620.12 and .A35-.A42)
Specialists may assist auditor in evaluating the sufficiency and appropriateness of audit evidence obtained in forming an opinion on the financial statements	No	Yes (AU-C-620.07 and .A5)	Yes (AU-C-620.07 and .A5)

Determining Whether to Involve Internal Specialist and/or Use Work of Expert Engaged by Auditor



We can Use the Work of Management's Expert as Audit Evidence ... depending on...

- The nature, scope, and objectives of the work of specialist
- Whether specialist is employed by entity or is party engaged to provide relevant services
- Extent to which management exercises control or influence or work of specialist
- Competence and capabilities of specialist
- Whether specialist is subject to technical performance standard or professional or industry requirements
- Auditor's ability to evaluate work and findings of specialist without assistance of auditor's specialist



Recognition of Changes in the Net Pension Liability (NPL)

–

$$\text{NPL} = \text{TPL} - \text{Assets}$$

Change in the NPL	Expense	Deferred Outflow or Inflow of Resources
Service cost	X	
Interest on TPL	X	
Plan changes	X	
TPL-related differences between expected and actual experience (e.g. change in expectancy, other actuarial changes beyond assumptions)	Single-period piece	Both active & inactive portion (with piece expensed) amortized over average expected remaining service life of active & inactive using closed end periods
TPL-related changes in assumptions	Single-period piece	Both active & inactive portion (with piece expensed) Same

Recognition of Changes in the NPL

(cont.)

Change in the NPL	Expense	Deferred Outflow or Inflow of Resources
Projected earnings on investments	X (reduction)	
Difference between projected and actual investment earnings	Single-period piece	X (with piece expensed over five years – closed period) Present on a net basis on the statement of plan net position / statement of net position
Other sources	X	

COUNTY EMPLOYEES RETIREMENT SYSTEM

County Employees Pension Plan

Statement of Fiduciary Net Position

June 30, 20X9

(Dollar amounts in thousands)

	20X9
Assets	
Cash and deposits	\$ 69,497
Securities lending cash collateral	170,055
Total cash	239,552
Receivables:	
Contributions	6,988
Due from broker for investments sold	59,777
Investment income	4,402
Other	114
Total receivables	71,281
Investments:	
Domestic fixed income securities	637,987
Domestic equities	1,006,595
International equities	430,486
Real estate	137,850
Total investments	2,212,918
Total assets	2,523,751
Liabilities	
Payables:	
Investment management fees	1,462
Due to broker for investments purchased	107,861
Collateral payable for securities lending	170,055
Other	7,265
Total liabilities	286,643
Net position restricted for pensions	\$ 2,237,108

Statement of Changes in Fiduciary Net Position for the Year Ended June 30, 20X9

(Dollar amounts in thousands)

	20X9
Additions	
Contributions:	
Employer	\$ 79,713
Member	31,451
Total contributions	111,164
Investment income:	
Net appreciation in fair value of investments	162,137
Interest and dividends	42,179
Less investment expense, other than from securities lending	(8,905)
Net income from investing, other than from securities lending	195,411
Securities lending income	989
Less securities lending expense	(246)
Net income from securities lending	743
Net investment income	196,154
Other	41
Total additions	307,359
Deductions	
Benefit payments, including refunds of member contributions	119,434
Administrative expense	3,373
Other	33
Total deductions	122,840
Net increase in net position	184,519
Net position restricted for pensions	
Beginning of year	2,052,589
End of year	\$ 2,237,108

What Plan financial statements will look like

STATE of MONTANA

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Illustration: Changes in NPL

	20X9	20X8	20X7	20X6	20X5
Total pension liability					
Service cost	\$ 101,695	\$ 100,317	\$ 103,471	\$ 98,685	\$ 81,657
Interest	231,141	219,193	200,491	185,434	171,179
Benefit changes	-	-	-	-	-
Differences between expected and actual experience	(69,638)	(41,374)	(9,387)	17,438	29,183
Changes of assumptions	-	-	63,375	-	-
Benefit payments	(124,083)	(118,311)	(109,281)	(99,654)	(91,558)
Refunds of contributions	(2,780)	(2,764)	(2,927)	(2,684)	(2,251)
Net change in total pension liability	136,335	157,061	245,742	199,219	188,210
Total pension liability—beginning	3,045,893	2,888,832	2,643,090	2,443,871	2,255,661
Total pension liability—ending (a)	\$3,182,228	\$3,045,893	\$2,888,832	\$2,643,090	\$2,443,871
Plan net position					
Contributions—employer	\$ 109,544	\$ 107,028	\$ 105,755	\$ 103,089	\$ 89,054
Contributions—member	51,119	50,344	54,949	51,926	41,411
Net investment income	199,273	83,235	(30,957)	131,629	236,486
Benefit payments	(124,083)	(118,311)	(109,281)	(99,654)	(91,558)
Administrative expense	(3,427)	(3,333)	(3,046)	(2,684)	(2,349)
Refunds of contributions	(2,780)	(2,764)	(2,927)	(2,684)	(2,251)
Other	8	(34)	37	9	(88)
Net change in plan net position	229,654	116,165	14,530	181,631	270,705
Plan net position—beginning	2,283,333	2,167,168	2,152,638	1,971,007	1,700,302
Plan net position—ending (b)	\$2,512,987	\$2,283,333	\$2,167,168	\$2,152,638	\$1,971,007
Net pension liability—ending (a) – (b)	\$ 669,241	\$ 762,560	\$ 721,664	\$ 490,452	\$ 472,864

Note: Only 5 years are presented here;
10 years of information would be required

STATE of MONTANA

Illustration: NPL

Components/Ratios Required

	<u>20X9</u>	<u>20X8</u>	<u>20X7</u>	<u>20X6</u>	<u>20X5</u>
Total pension liability	\$ 3,182,228	\$ 3,045,893	\$ 2,888,832	\$ 2,643,090	\$ 2,443,871
Plan net position	(2,512,987)	(2,283,333)	(2,167,168)	(2,152,638)	(1,971,007)
Net pension liability	<u>\$ 669,241</u>	<u>\$ 762,560</u>	<u>\$ 721,664</u>	<u>\$ 490,452</u>	<u>\$ 472,864</u>
Ratio of plan net position to total pension liability	78.97%	74.96%	75.02%	81.44%	80.65%
Covered-employee payroll	\$ 435,373	\$ 432,256	\$ 426,939	\$ 412,280	\$ 387,055
Net pension liability as a percentage of covered-employee payroll	153.72%	176.41%	169.03%	118.96%	122.17%

Note: Only 5 years are presented here;
10 years of information would be required

Illustration: Contribution-related Information Required if ADC done

	20X9	20X8	20X7	20X6	20X5
Actuarially calculated employer contribution	\$ 109,544	\$ 107,028	\$ 105,755	\$ 103,089	\$ 89,054
Actual employer contributions	<u>(109,544)</u>	<u>(107,028)</u>	<u>(105,755)</u>	<u>(103,089)</u>	<u>(89,054)</u>
Annual contribution deficiency (excess)	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>
Covered-employee payroll	\$ 435,373	\$ 432,256	\$ 426,939	\$ 412,280	\$ 387,055
Actual contributions as a percentage of covered-employee payroll	25.16%	24.76%	24.77%	25.00%	23.01%

Note: Only 5 years are presented here;
10 years of information would be required

Special Funding Situations (SFSs) (i.e. Teachers in STRS?)

- Nonemployer entity is legally responsible for contributions to a pension plan used to provide pensions to government employees
- A form of on-behalf payment
- Guidance proposed related to both defined benefit and defined contribution SFSs

Types of SFSs

- Conditional on one or more events or circumstances unrelated to the pensions
 - Example: requirement to contribute a portion of a given revenue source
- Unconditional
 - Example: Requirement to contribute a specified proportion of payroll
 - Example: Requirement to contribute a defined portion of the employer's required contributions

Conditional SFS

- Governmental nonemployer contributing entity (GNCE) (i.e. State) recognizes its contributions in accordance with Statement 24 (grant expense/expenditure)
- *Employer* recognizes *grant revenue* in amount of NCE contribution and follows all other requirements of the Exposure Draft for pension expense/liability
- Employer notes/RSI identify employer contributions by source (direct vs. on behalf)

Unconditional SFS:

Defined Benefit – GNCE (i.e. State)

- Recognize proportionate share of:
 - NPL, pension expense, deferred outflows of resources, and deferred inflows of resources
 - Share of employer pension expense is classified as grant expense
- Proportion determined in same way as cost-sharing employer proportion
- Same entity-specific accounting as for cost-sharing employers



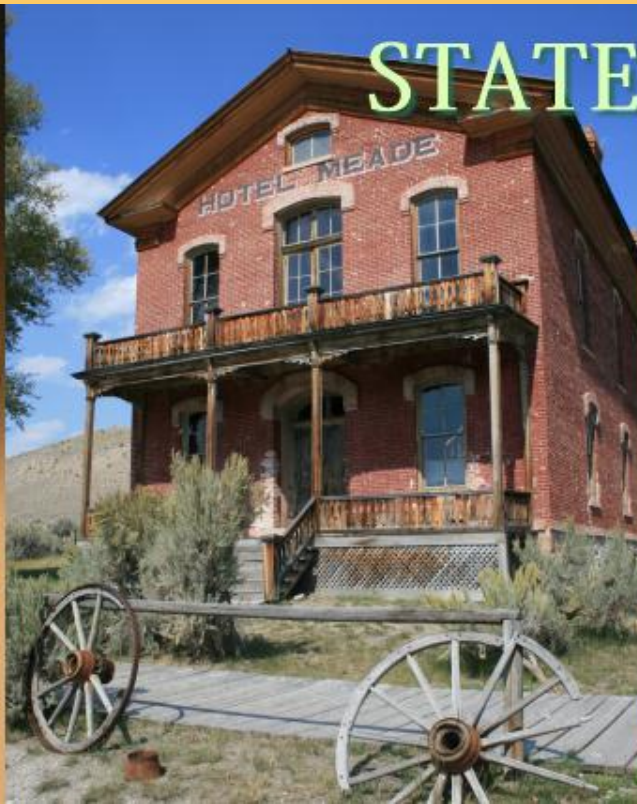
Unconditional SFS: Defined Benefit—Employer

- NPL, deferred outflows of resources, and deferred inflows of resources reduced by Non-contributory employer (NCE)'s proportionate share
- Pension expense recognized without reduction
- Grant revenue recognized in amount of NCE's grant expense

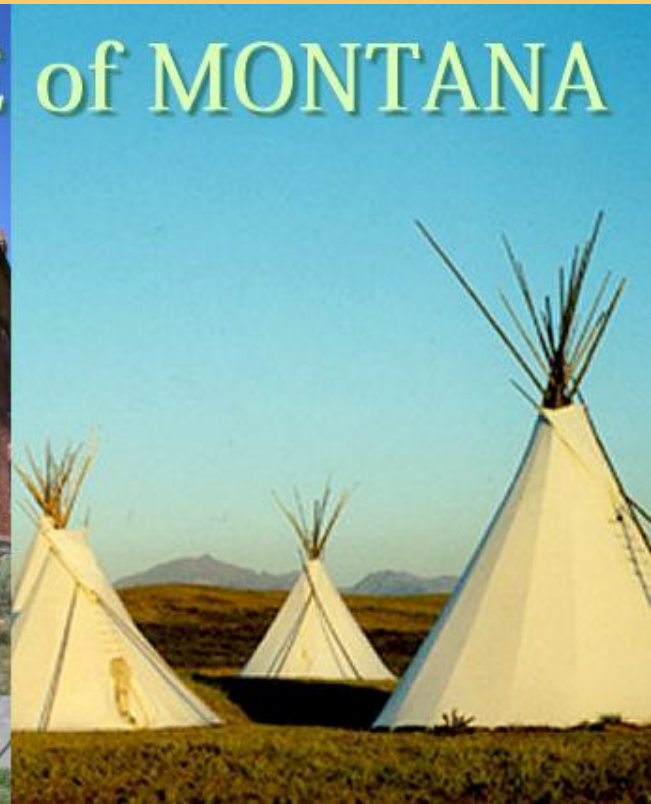
Best Practices in Implementation of the new Pension Standards



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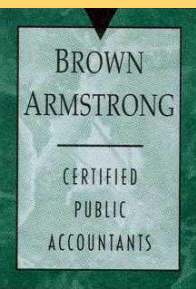


STATE of MONTANA



Best Practices in Implementation

- Key Worries to be Addressed as part of Implementation per GASB Letter to the Profession
 - Pension funding policy
 - Selection of assumptions
 - Timing of measurements
 - Timing of actuarial valuations
 - Development of information for employer reporting



Best Practices in Implementation

- Funding Policy
 - Statements remove the direct link between measurements for funding purposes and measurement of pension expense for accounting and financial reporting purposes. For governments that have actuarially based funding policies, the measurement requirements of the new Statements for financial reporting purposes will include an actuarial valuation likely different from (and in addition to) the actuarial valuation that is used for funding purposes.
 - Address through Consistent Communication



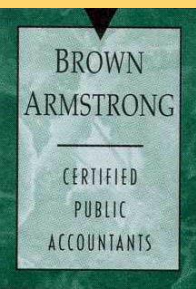
Best Practices in Implementation

- Selection of Assumptions
 - Coordination will be necessary between pension plans and employers when measurements of the net pension liability of the employers are made. Assumptions integral to the measurement of an employer's pension liability include the long-term expected rate of return on pension plan investments, which plays a potentially significant role in the determination of the discount rate.
 - Address through Communication, alignment of all actuarial assumptions to expectations of employers

Best Practices in Implementation

- **Timing of Measurements**

- Issue will be requirement to present information about the liabilities of the employers, the net pension liability is required to be measured as of the end of Plan's fiscal year.
- Employers are provided with additional flexibility with regard to the “as of” (or “measurement”) date of the net pension liability reported in its financial statements each period.
 - Employer may report a pension liability measured between the end of the employer's prior fiscal year and its current fiscal year-end (for example, as of the pension plan's fiscal year-end). Because information about pension plan net position is needed to measure the employer's net pension liability, in pension plans in which the same fiscal year-end is not shared among the employers and the plan itself, coordination of the employers' measurement date will be necessary.
- **Address through coordination and timely transmittal of information to members**



Best Practices in Implementation

- Timing of Actuarial Valuations
 - Should not be an issue with as long as annual valuations are performed
 - If Plan and employer fiscal year-ends are different, attention to the timing of the actuarial valuation date relative to those fiscal year-ends will be necessary to ensure that the actuarial valuation date, in conjunction with the measurement date (discussed above), will fall within the timing requirements of the new Statements.
 - Again – shouldn't be a problem



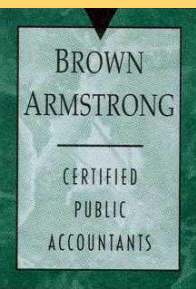
Best Practices in Implementation

- Development of Information for Employer Reporting
 - **Key concern for Plans**
 - RSI schedule information (up to 10 years prior)
 - Additional information on cost sharing employer information expense
 - **Key Questions**
 - Who prepares it?
 - When is it released?
 - Is it auditable?



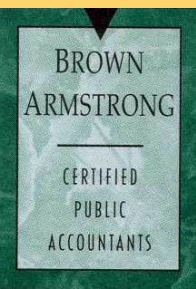
Best Practices in Implementation

- Development of Information for Employer Reporting
 - Questions *may* be answered by some / all of the following:
 - Implementation Guide(s)
 - AICPA Update to State & Local Audit Guide (new pensions chapter coming **but not until 2014**)
 - Task force coordination at each plan
 - But – who pays for it?



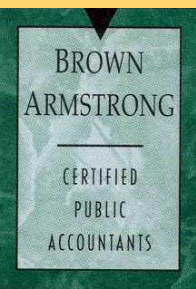
Best Practices in Implementation

- Key additional question for Cost Sharing Plans
 - Information to determine employers' proportionate shares needs to be tested and agreed upon
 - Net pension liability and other elements are dependent on it
 - Standard encourages that each employer's projected long-term relative share of contributions to the plan as the basis for establishing each employer's proportion
 - Address through dry runs, communication



Reminder - Auditing Provisions *May* Be

- Cost sharing schedule for all employers may be required by AICPA even though not in GASB-67
 - Schedule includes all elements for all employers
 - Key risks audited including census data, benefit payments, posting of investment return to accounts etc.
 - Full guidance not until 2014



Best Practices of Implementation

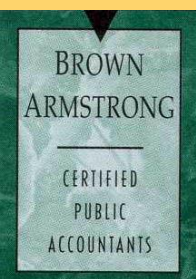
- Some Plans are using a task force
 - Plan administration / controller
 - Plan auditor
 - Plan actuary
 - Employers' controller staff
 - Employers' auditor(s)
- Goals
 - Communication and documentation of decisions (see above)
 - Understanding of timeline
 - Roles & responsibilities
 - Uniformity in presentation



Potential Timeline

- Example: Employers need to go to those charged with governance on October 31st annually – start at due date and work *backwards*. The plan has a year end of December 31.

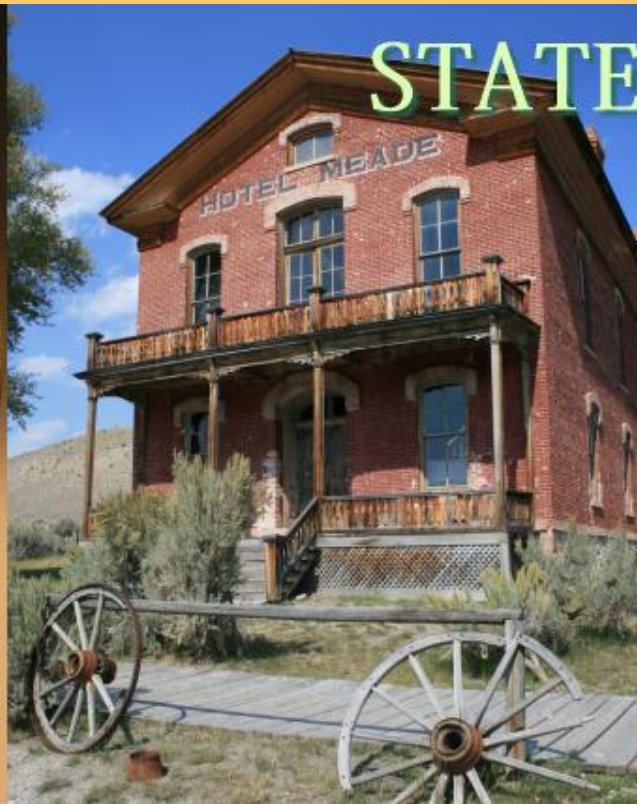
Date	Potential Action
10/31/15	Members' financials submitted to Boards
6/30/15	First fiscal year of new pension standards for members (GASB-68)
5/31/15	Plan information to Members
4/30/15	Actuarial valuation reporting date (as of 12/31/14)
12/31/14	Plan Year End under GASB-67
1/1/14	Plan Year beginning under GASB-67
5/30/13	30 month cutoff of data allowable under GASB-67



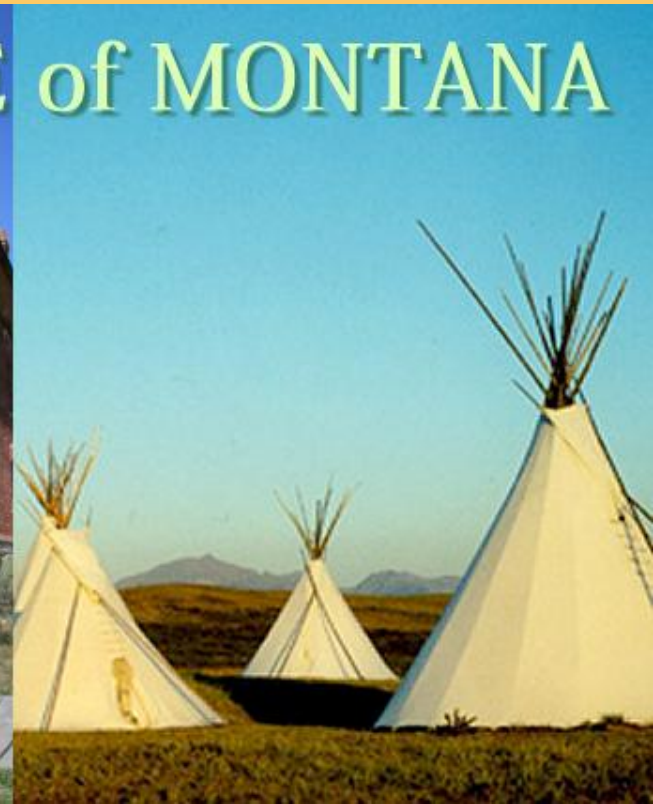
Discussion – What does this all mean?



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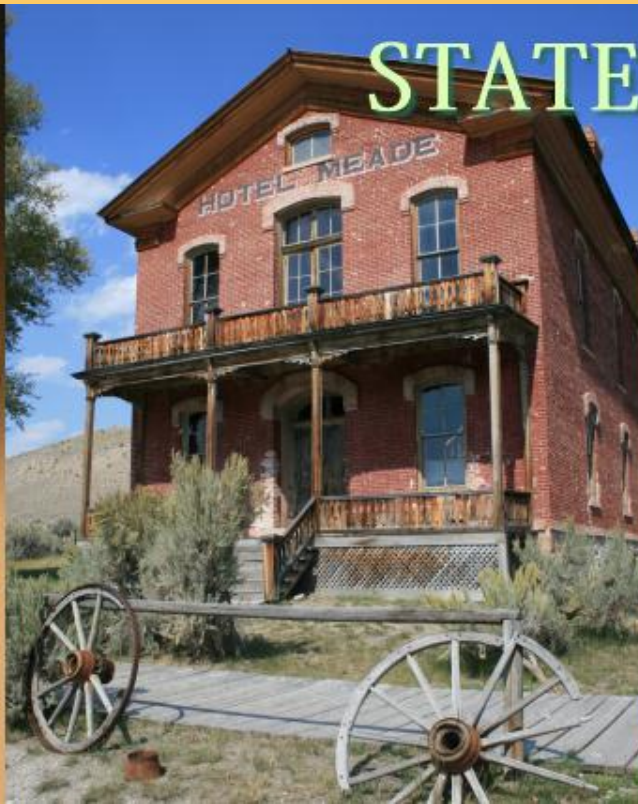
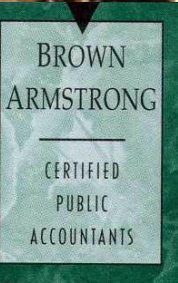
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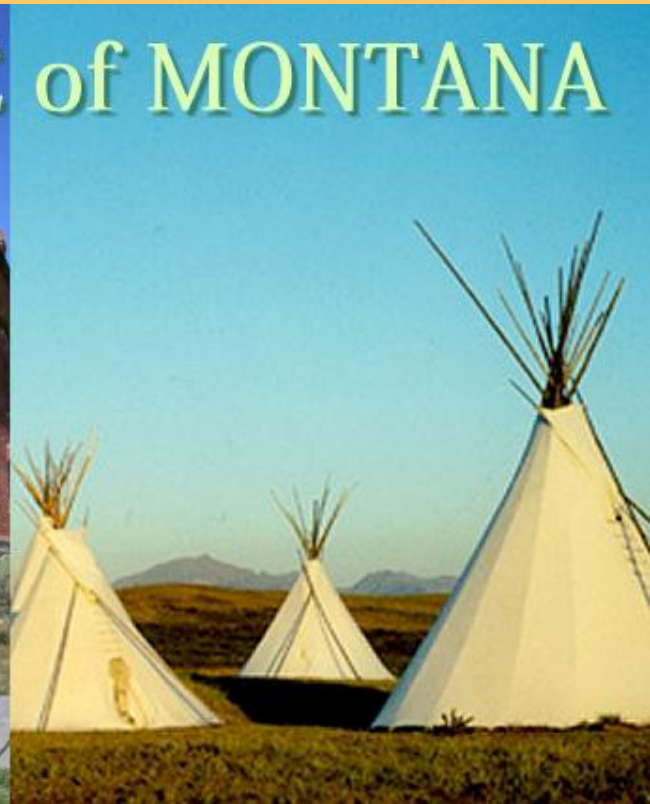
Government combinations and disposals of operations



GASB Statement No. 69



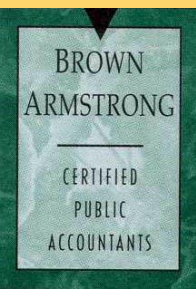
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Background

Applicable guidance after issuance of Statement 62:

- APB 16 and 17 (Pre-89)
- FASB 141(and revisions)
- FASB 164
- APB 30 (Pre-89)



Scope

- Combinations in which insignificant or no consideration is provided
 - Government mergers
 - Transfers of operations
- Combinations in which significant consideration is provided
 - Government acquisitions
- Disposal of government operations



Terminology

- Government combinations are identified by the continuance of the provision of services involved
- **Government merger**—two or more separate legal entities combine to form a new entity, and one or more of the prior entities cease to exist
 - Insignificant or no consideration exchanged



Terminology

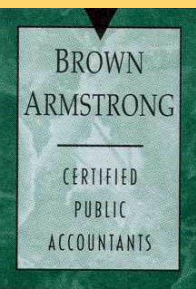
- **Government acquisition**—one government acquires another entity (or its operations) in exchange for significant consideration
- Operations are integrated set of activities conducted and managed for the purpose of providing identifiable services with associated assets or liabilities
- Disposals of operations involve less than a legally separate entity and insignificant or no consideration`



Mergers—New Government

$$A + B = C$$

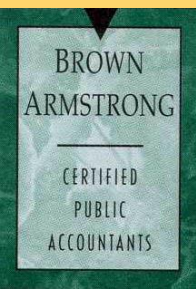
- Merger date is the date the combination becomes effective and the beginning of the reporting period when a new government is created
- Assets, liabilities and deferrals at carrying values
 - Presumption of GAAP
- Adjustments
 - Accounting principles, policies, and estimates
 - Capital asset impairment
 - Transaction eliminations



Mergers—Continuing Government

$$A+B = A$$

- Merger date is the beginning of the reporting period of the continuing government in which the combination occurs, regardless of the date the merger takes place
- Assets, liabilities and deferrals at carrying values
 - Presumption of GAAP
- Adjustments
 - Accounting principles, policies, and estimates
 - Capital asset impairment
 - Transaction eliminations



Acquisitions

- Acquisition date is the date on which the acquiring government gains control of the assets and becomes obligated for the liabilities of the acquired government
- Assets, liabilities and deferrals measured at *acquisition value*—a market-based entry price
- Exceptions to acquisition value—employment benefit arrangements

Acquisitions

- Measure consideration as the value of assets conveyed or liabilities incurred to the former owner
- Accounting for the difference between acquisition value and consideration:
 - $\text{Consideration} > \text{AV} \rightarrow$ deferred outflow of resources
 - $\text{AV} > \text{consideration} \rightarrow$ reduction of noncurrent assets or contribution received
- Recognize acquisition costs as expenses

Intra-Entity Acquisitions

- Recognize assets, liabilities, and deferrals at carrying value
- Difference between acquisition price and carrying value:
 - Special items in acquirer's own statements
 - Transfer or subsidy, as appropriate, in statements of the reporting entity

Disposals of Operations – sales / spinoffs – new governments

- Transferee should measure assets, liabilities and deferrals at carrying value
- Transferor reports a gain or loss as a special item—should consider all costs directly associated with disposals of operations
- Disclosure
 - Description of the circumstances leading to the discontinuation
 - Operations revenues, expense, and non-operating items

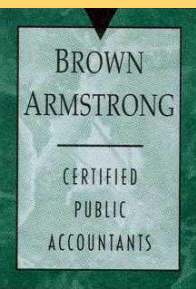
Disclosures

- *All* combinations
 - Brief description of the combination and identification of the entities involved
 - Date of the combination
 - Primary reasons for the combination
- Mergers and transfers of operations
 - Carrying values recognized as of the merger date
 - Description of significant adjustments
 - Amounts recognized



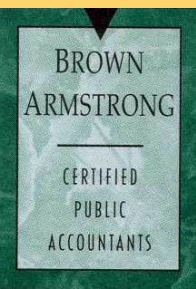
Disclosures

- Acquisitions
 - Brief description of consideration provided
 - Total amount of net position acquired
 - Brief description of contingent consideration arrangements



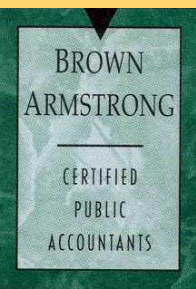
Effective Date

- Effective for periods beginning after December 15, 2013 – for June 30th – July 1, 2014



Practical Ways to Implement GASB-69

- Implementation is prospective not retroactive so if one has occurred, no need to restate
- GASB-69 is one of those statements that it's not needed unless you have it occur but it occurs more often than you may think!
- If one is in process, figure out what type it is and see if you can make sure legislation / agreement aligns to GAAP
 - Auditing of a merger at wrong time could be ugly!



A Real Example

- The school districts of Nevada City and Grass Valley California have discussed a merger –
 - The unified school district began operations January 1, 2013, and was formed from the merger of the two former school districts to take advantage of the cost efficiencies based on the elimination of redundant services pursuant to the citizens' approval of a referendum including the Consolidation Plan. The initial opening balances of assets, deferred outflows of resources, liabilities, deferred inflows of resources, and net position, as of the beginning of the period, were determined on the basis of the carrying values reported in the separate financial statements of December 31, 2012 were as follows:



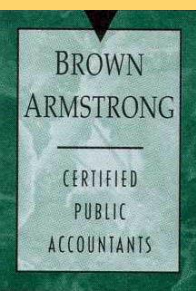
	Nevada City	Grass Valley	Total	Adjustments		Total
				Debit	Credit	
ASSETS						
Current assets	\$ 67,685,010	\$ 67,987,262	\$ 135,672,272	\$ —	\$ —	\$ 135,672,272
Capital assets	321,411,511	317,415,552	638,827,063	—	4,000,000	634,827,063
Other assets	448,823	250,000	698,823	—	80,000	618,823
Total assets	389,545,344	385,652,814	775,198,158	—	4,080,000	771,118,158
DEFERRED OUTFLOWS OF RESOURCES						
Accumulated decrease in fair value of hedging derivatives	—	127,520	127,520	—	—	127,520
LIABILITIES						
Current liabilities	22,632,625	19,308,605	41,941,230	—	—	41,941,230
Noncurrent liabilities	157,784,651	91,463,340	249,247,991	—	—	249,247,991
Total liabilities	180,417,276	110,771,945	291,189,221	—	—	291,189,221
DEFERRED INFLOWS OF RESOURCES						
Accumulated increase in fair value of hedging derivatives	—	1,040,482	1,040,482	—	—	1,040,482
NET POSITION						
Net investment in capital assets	176,799,960	222,799,960	399,599,920	4,000,000	—	395,599,920
Restricted	24,203,913	49,985,155	74,189,068	—	—	74,189,068
Unrestricted	8,124,195	1,182,792	9,306,987	80,000	—	9,226,987
Total net position	\$ 209,128,068	\$ 273,967,907	\$ 483,095,975	\$ 4,080,000	\$ 4,080,000	\$ 479,015,975

Question – why the \$4 million adjustment? The \$80k adjustment was for inventory of supplies and materials changes.

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Let's try another one

- County Fire Department (CFD) is a separate municipal corporation, organized as a regional fire protection service authority. Under an intergovernmental agreement between the City (City) and the CFD, the City will combine its fire protection operations with the CFD for the purpose of providing services to the City's citizens. On March 15, 2014, the City transferred the assets and liabilities comprising its fire service operations to the CFD. The City transferred an administrative building, fire stations, engines, trucks, and various other equipment having a carrying value of \$6.3 million. The CFD will also assume \$3.4 million of the City's long-term debt related to fire service operations. There are no deferred outflows of resources or deferred inflows of resources associated with the City's fire service operations.

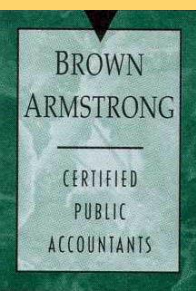


Accounting and Disclosure

The assets and liabilities transferred to the CFD represent an integrated set of assets and liabilities managed for the purpose of providing fire services, thus meeting the definition of an operation. In addition, service continuation is presumed because the assets used by the City to provide fire services will be used in a similar manner by the CFD to provide a similar service. There is no consideration given in the transaction.

What would the special item be on the CFD's books and as of what date? Also where would it land up in the statement of net position? (Think back to earlier discussion on GASB-63)

What would the City recognize?



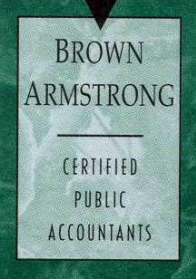
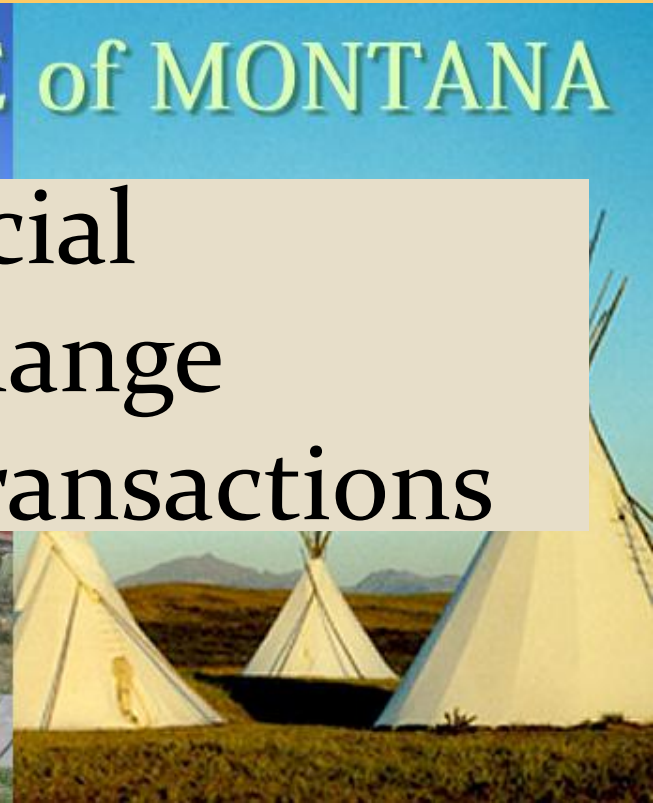


GASB-70

HOT OFF THE PRESSES

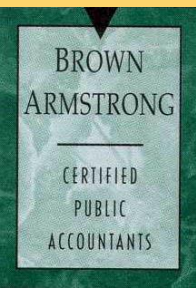
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Accounting and Financial Reporting for Nonexchange Financial Guarantee Transactions



Financial Guarantees

- Financial Guarantees are Numerous (especially for a state)
 - Lower levels of government (Cities, districts etc)
 - Not for profits
 - Private corporations
 - Individuals
 - What could be some that you know about?



Financial Guarantees

- Non-exchange transaction – no direct consideration equal to value provided
- Government commits to paying an obligation if the holder does not pay



Financial Guarantees

- Other Items
 - Does not apply to Special Assessments (GASB-6) but calls into question whether or not it should – potential future project
 - Amends portions of GASB-10 (Risk – Insurance), GASB-33 and GASB-62

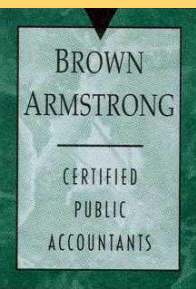
Financial Guarantees

- Key Elements
 - The government that extends a non-exchange financial guarantee will recognize a liability when qualitative factors *or* historical data indicate that it is *more likely than not* that the government will make a payment on the guarantee
 - Amount of liability = best estimate of future cash flows to be incurred
 - If no best estimate, then use minimum amount in range
 - Similar to GASB-49



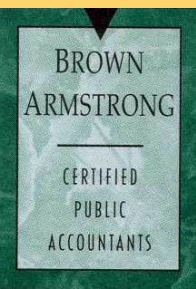
Qualitative Indicators of Liability

- Initiation of the process of entering into bankruptcy or a financial reorganization
- Breach of a debt contract in relation to the guaranteed obligation, such as
 - Failure to meet rate covenants,
 - Failure to meet coverage ratios,
 - Default or delinquency in interest or principal payments



Qualitative Indicators of Liability

- Indicators of significant financial difficulty, such as
 - Failure to transfer deposits from debt service funds to paying agents or trustees;
 - Out of Ordinary draw on a debt service reserve fund;
 - Initiation of the process by a creditor to intercept receipts to make a debt service payment;
 - Debt holder concessions;
 - Significant investment losses;
 - Loss of a major revenue source;
 - Significant increase in noncapital disbursements in relation to operating or current revenues;
 - Commencement of financial supervision by another government
- Also consider default ratios, **history – history is very important in pools of loans / guarantees**



Recognition

- *More Likely Than Not* threshold is 50%
- Recognition in Full Accrual statements
 - Amount recognized = best estimate of discounted PV of cash flows expected to incur due to guarantee
 - If no best estimate in a range, pick the minimum
- In Governmental Funds
 - Amount = funds to be expended with current financial resources

Government Issuing a Guaranteed Obligation

- Entity wide and Governmental Funds:
 - If a government is required to repay a guarantor for nonexchange financial guarantee payments made on the government's obligations, the government should reclassify that portion of its previously recognized liability for the guaranteed obligation as a liability to the guarantor.
 - The government that issued the guaranteed obligation should continue to report its liability until that portion of the liability is legally released, such as when a Plan of Adjustment is confirmed by the court in the case of bankruptcy.
 - Upon release of liability - REVENUE



Wrinkle for Blended Component Units – NOT Discrete

- When a government that extends a nonexchange financial guarantee recognizes a liability for the guarantee:
 - The government that issued the guaranteed obligation should recognize a receivable equal to the amount of the liability recognized by the government that extended the guarantee, if the government that issued the guaranteed obligation is:
 - A blended component unit of that government
 - A primary government that includes the government that extended the guarantee as a blended component unit within its reporting entity
 - Within the same reporting entity and both parties are blended component units of the same primary government.



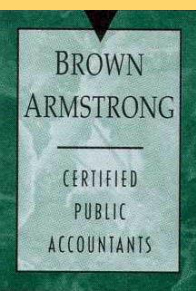
Financial Guarantees

- Other Key Elements of GASB-70
 - Typical disclosures (who, what, when, how much etc.)
 - Liability is reported until either paid or released by the obligor (entity holding the liability)
 - If released – revenue recognized upon release
 - Note disclosure on guarantees will be required similar to commitments
 - **Implementation is periods beginning after June 15, 2013 (July 1)**
 - Retroactive restatement required



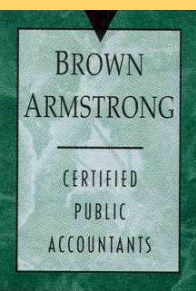
Try a Real Example

- **Facts and assumptions:** A State extends nonexchange financial guarantees for qualifying bonds issued by school districts within the State for construction of schools in accordance with the School Construction Act. Central State has determined based on historical evidence that 0.25 percent of the total amount of nonexchange financial guarantees extended eventually require a guarantee payment to be made, and 50 percent of guarantee payments made are recovered from the school district.
- At July 1, 2015, The State has recognized liabilities of \$18.5 million related to \$14.6 billion in nonexchange financial guarantees outstanding with varying dates of maturity through June 30, 2036. During the fiscal year ending June 30, 2016, \$1.245 billion of the guaranteed obligations are repaid by the school districts that issued the obligations while the State pays \$5 million on bond obligations of several school districts that did not make their required payments.



Try a Real Example

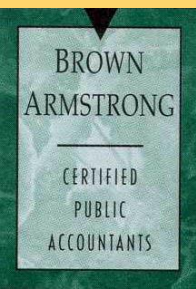
- Considering payments made during the current year in relation to the historical average of school districts that default, The State estimates that its liability related to nonexchange financial guarantees will increase by \$1.875 million for nonexchange financial guarantees outstanding at June 30, 2016. The increase in present value of the prior liability for the fiscal year ending June 30, 2015, is \$1.5 million. In addition, during the fiscal year ending June 30, 2016, The State extends \$900 million in nonexchange financial guarantees on bonds issued *for* school construction with varying dates of maturity through June 30, 2037.



Questions

- What would the increase in the liability be for the year?
- What happened to the liability for the payment of \$5 million paid in principal and interest?
- What about the \$1.875 million?

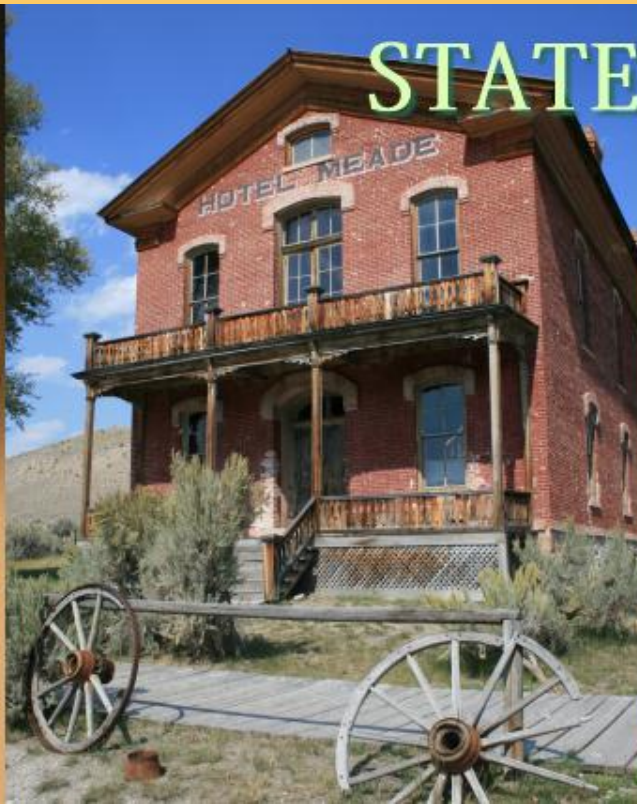
Beginning of Year	Increases	Decreases	End of Year
\$18,500,000			



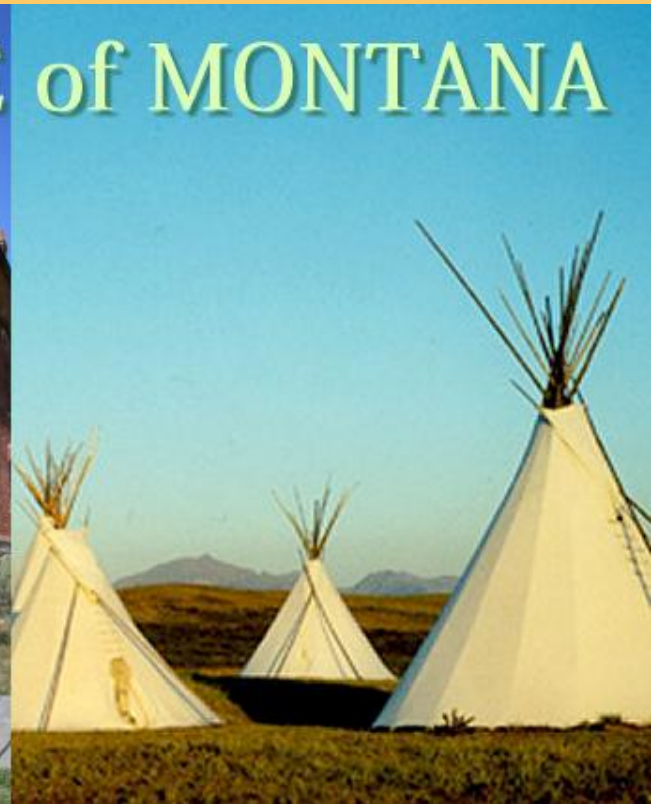
Other GASB Projects



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Other Projects in Process

- Recognition and Measurement Concepts (PV)
- Fair Value—Measurement and Application
- Other Postemployment Benefits
- **New - Leases**
- GAAP Hierarchy
- FAF project on GASB's Scope of Authority

Updated Potential Calendar

PROJECT	Exposure Draft	Final Standard
Conceptual Framework – Measurement	June 2013	March 2014
Pensions Technical Correction	June 2013	December 2013
Implementation Guide – Pensions (Plans)		June 2013
Fair Value Measurement and Application	Preliminary Views – June 2013 / Exposure Draft June 2014	December 2014
2013-2014 <i>Comprehensive Implementation Guide</i>	N/A	September 2013
Conceptual Framework – Recognition	March 2014	March 2015
GAAP Hierarchy	February 2014	June 2015
Implementation Guide – Pensions (Employers)	N/A	March 2014
OPEB	April 2014	June 2015
Leases	December 2014	December 2015

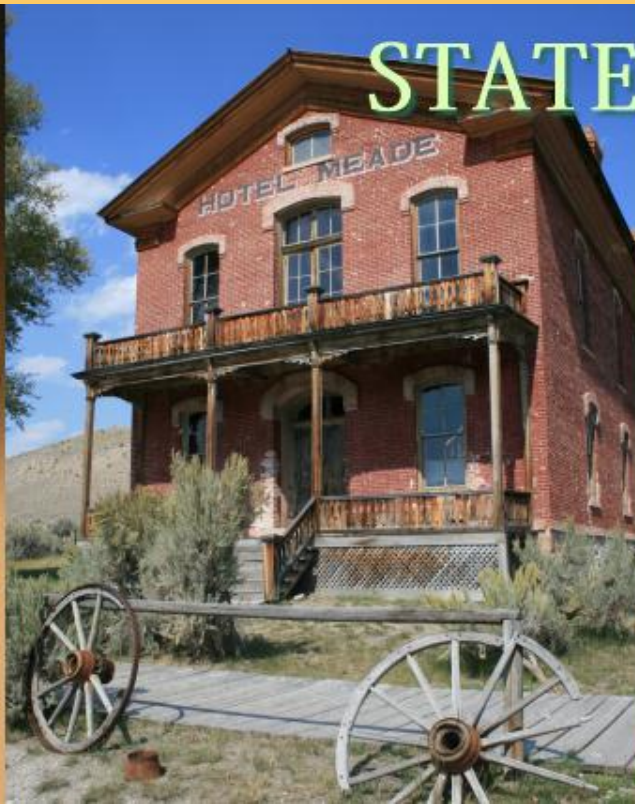
*Economic Condition Project on Indefinite Hold – FAF Project
Implementation not disclosed*

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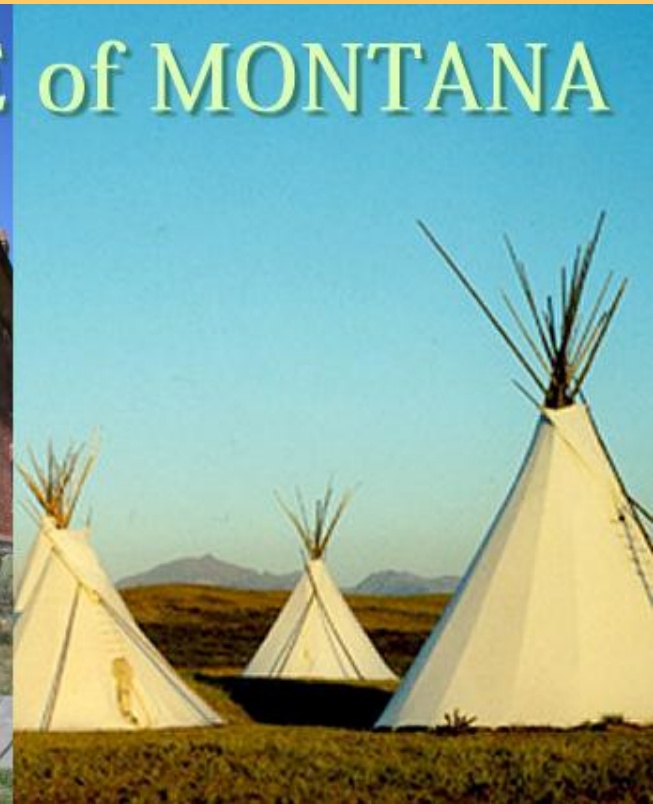
GASB's Conceptual Framework Project Recognition and Measurement



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Where is the Project Now?

- Project has been split into two projects
 - Recognition Project
 - What are the fundamental recognition criteria necessary to report an element in a financial statement?
 - Measurement Project
 - What measurement approach(es) best conveys the message(s) intended for financial statements? What is the role of initial amounts and remeasured amounts in conveying these messages? Is the same measurement approach applicable in all measurement focuses?
 - Should the application of remeasured amounts be different for the statement of net position and the statement of activities? How do remeasured amounts relate to the cost of service model of the statement of activities?



Where is the Project Now?

- Project has been split into two projects
 - Both Projects
 - What messages are financial statements conceptually attempting to convey? (In other words, what is the story that the financial statements attempt to communicate, or what questions should be answered by reading different financial statements and financial statements prepared using different measurement focuses? For example, the statement of cash flows answers the question, “What happened to cash during the year?”)
 - What is the relationship among objectives of financial reporting (user needs), financial statements, measurement focuses, and measurement approaches at the conceptual level?
 - How does when an element is recognized affect the meaning that is to be conveyed by a particular financial statement?



Key Project Decisions

- Since 2008, the Board has consistently reaffirmed two key definitions in measurement:
 - *Initial Transaction Date-based Measurement (Initial Amount)*—The transaction price or value assigned when an asset was acquired or a liability was incurred, including subsequent modifications to that price or value, such as through amortization or depreciation.

Current Financial Statement Date based Measurement (Remeasured Amount)—The value of an asset or liability remeasured as of the financial statement date, including fair value; current acquisition, sale, and settlement price; replacement cost; and value-in-use.

Based on the PV's responses

- The Board has affirmed the definition (remarkably) of economic resources measurement focus (full accrual) as:
 - The basis of accounting that incorporates all outflows of resources and inflows of resources and all assets, liabilities, deferred outflows of resources, and deferred inflows of resources.
 - Decisions about what is an asset / liability etc similar to GASB-65.

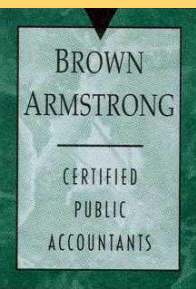


Based on the PV's responses

- By doing so – you have the following:
 - The objective of measurement then is to establish a framework for when each of the two primary measurement approaches (initial amounts and remeasured amounts) should be used.
 - A single measurement approach need not be applied to all assets and liabilities (think of capital assets and inventory for example)
 - The overriding criterion in evaluating the measurement approaches is which one best promotes achievement of the applicable objectives of financial reporting, with consideration of the qualitative characteristics of information in financial reporting.

Based on the PV's responses

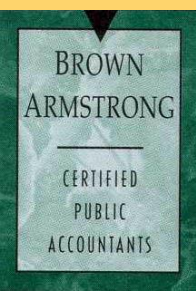
- Therefore, you have 4 types of measurement:
 - **Historical Cost (Proceeds)**—The amount paid to acquire an asset or the amount received pursuant to the incurrence of a liability in an actual exchange transaction.
 - **Fair Value**—The price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date.
 - **Settlement Amount**—The amount at which an asset could be realized or a liability could be liquidated with the counterparty, rather than through an active market.
 - **Replacement Cost**—The price that would be paid to acquire the service potential the entity will obtain from an asset in an orderly market transaction at the measurement date.



What's Left

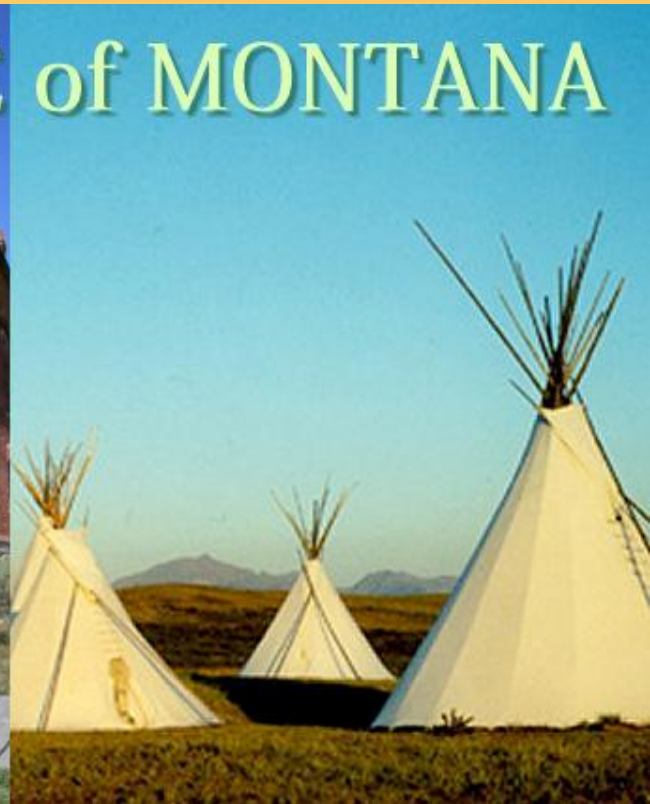
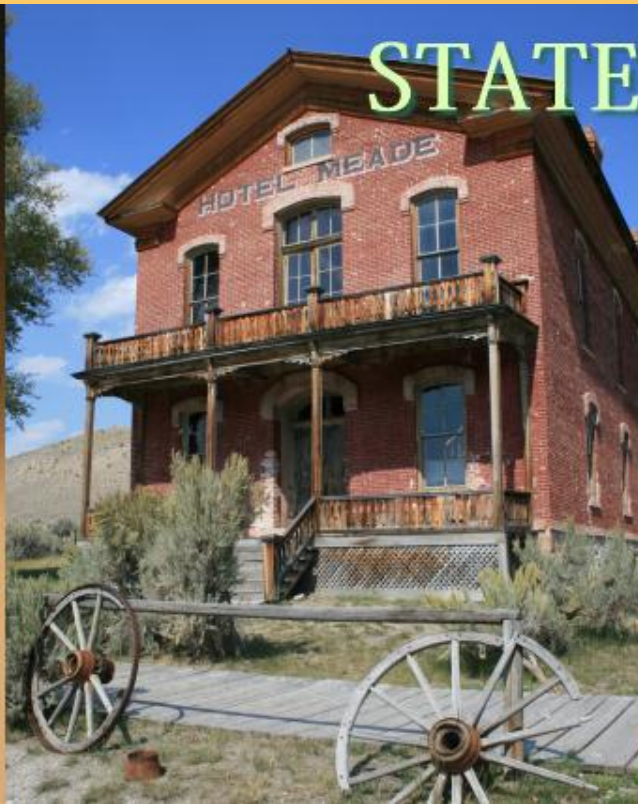
	Measurement Approaches	Recognition
Exposure Draft	June 2013	March 2014
Comment Period through	September 2013	June 2014
Redeliberation	To January 2014	To December 2014
Final Concepts Statement	March 2014	By January 2015

Remember why these are important – could point toward future standards on when to recognize assets, liabilities, inflows, outflows and deferrals



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Fair Value Measurement and Application



Fair Value Measurement and Application

- Goal
 - Review and consider alternatives for the further development of the definition of fair value,
 - Review the methods used to measure fair value, and potential disclosures about fair value measurements.
 - **KEY** - Measurement of alternative investments
 - ED perhaps by June 2013



Key Elements

- FASB ASC-820, *Fair Value Measurements and Disclosures* largely followed
 - Key issues
 - Investments and what is an investment
 - What guidance should be provided for appropriate methods and inputs for the development of fair values?
 - For the development of fair value estimates, should there be a hierarchy of inputs, such as between market-observed prices and model-based information?
 - Should all investments reported by governments be measured at their fair values?
 - What fair value disclosures are appropriate?

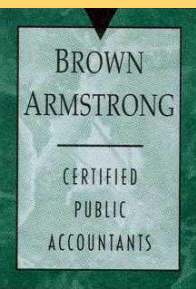


Key Decision Points

- If the asset provides a government service, Board will likely continue historical cost
 - If for investment return – fair value
 - Example – Mortgage Loans
 - Lending assets held primarily for the purpose of income or profit and that have present service capacity based solely on their ability to generate cash, to be sold to generate cash, or to procure services for the citizenry (the proposed definition of an investment) tentatively classified as investments.
 - Example – Donated Assets
 - Entry (Acquisition Value) rather than fair value
 - Watch out for Natural Resources!

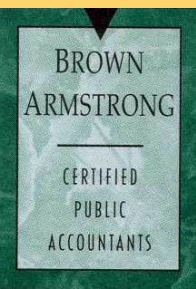
Various Approaches to Fair Value

- **Market Approach** – Quoted prices in active markets for identical or comparable assets or liabilities
 - Can include matrix pricing
- **Income Approach** – Techniques to convert future amounts to a single present amount.
 - Can include present value, option-pricing, and multi-period excess earnings
- **Cost** – replacement cost – does not apply to financial assets and liabilities



Explanation of Inputs per the Fair Value Standards

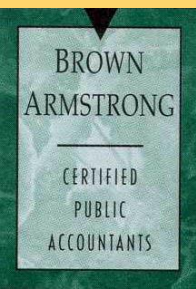
- **Observable inputs** – inputs from independent sources on what market participants would use – e.g. what does the *Wall Street Journal* say?
- **Unobservable inputs** – entity's own interpretation about the assumptions market participants would use



Explanation of Inputs per the Fair Value Standards (continued)

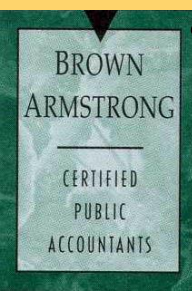
- *Level 1 Inputs* - Quoted prices (unadjusted) in active markets for identical assets and liabilities.

Valuations of these instruments do not require a high degree of judgment since the valuations are based on readily available quoted prices in active markets.



Explanation of Inputs per the Fair Value Standards (continued)

- *Level 2 Inputs* - Quoted prices for similar assets or liabilities in active markets; quoted prices for identical or similar assets or liabilities that are not active; and inputs other than quoted prices that are observable, such as models or other valuation methodologies. Valuations in this category are inherently less reliable than quoted market prices due to the degree of subjectivity involved in determining appropriate methodologies and the applicable underlying assumptions.



Explanation of Inputs per the Fair Value Standards (continued)

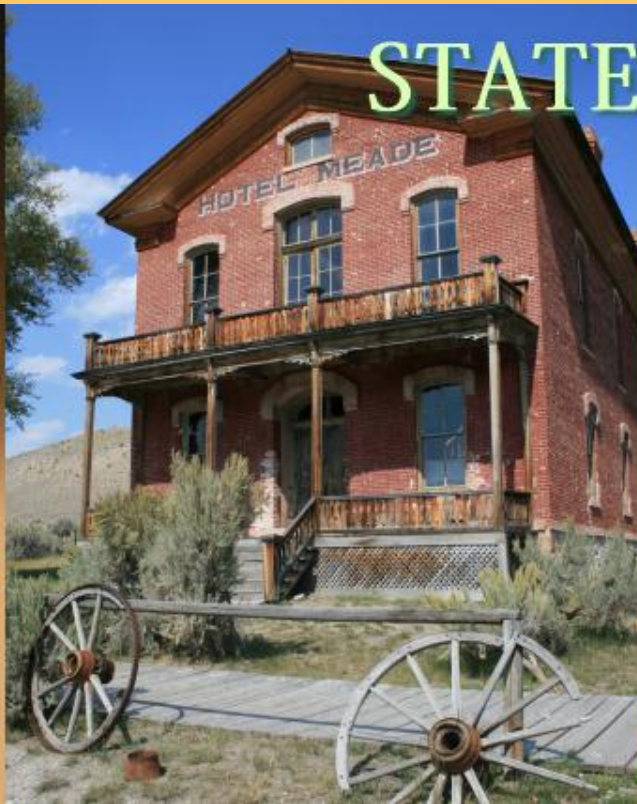
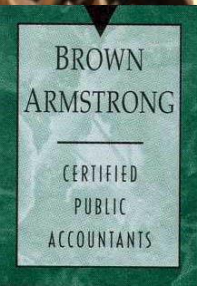
- *Level 3 Inputs* - Unobservable inputs for the valuation of the asset or liability. Level 3 assets include investments for which there is little, if any, market activity. These inputs require significant management judgment or estimation. These financial instruments have inputs that cannot be validated by readily determinable market data and generally involve considerable judgment by management.

Disclosures

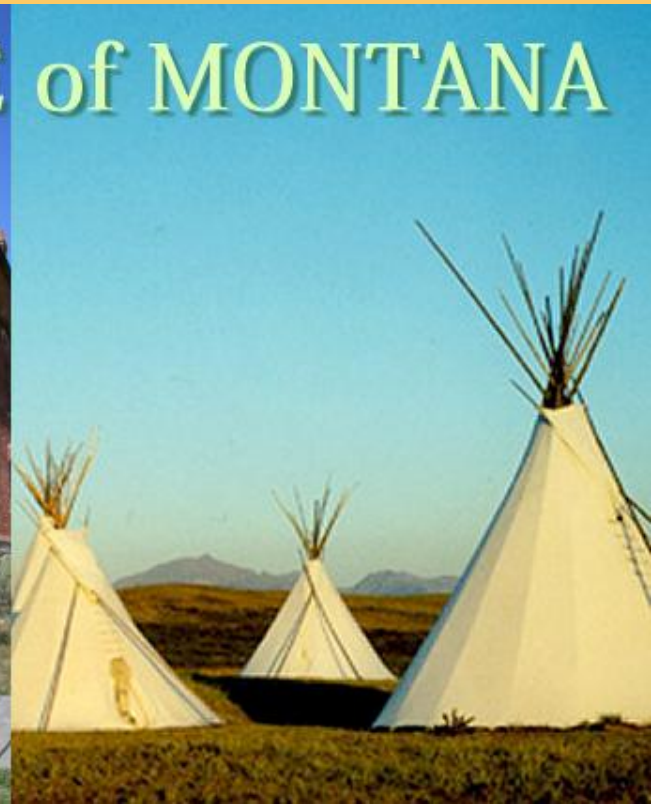
- Could be
 - Valuation techniques and inputs, replacing existing disclosures of methods and significant assumptions
 - The effect of the measurements on investment income for recurring fair value measurements using significant Level 3 unobservable inputs – could be sensitivity analysis
 - Additional fair value disclosures for investments in certain entities that calculate net asset value per share (or its equivalent) (**Watch out for SEC changes on Money Market Funds! (A \$1 is *not* \$1.)**)



OPEB Alignment

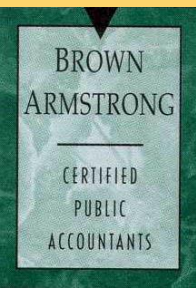


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OPEB Alignment

- Key Question – is it still a liability?
 - Other key elements
 - Alignment with GASB-67 / 68
 - Discount rate
 - 1 method of actuarial valuation
 - Agent / Cost sharing aspects
 - Building of a liability through service
 - Key variations
 - Certain OPEB plans allow return of assets at full funding
 - Certain OPEB plans are only subsidies



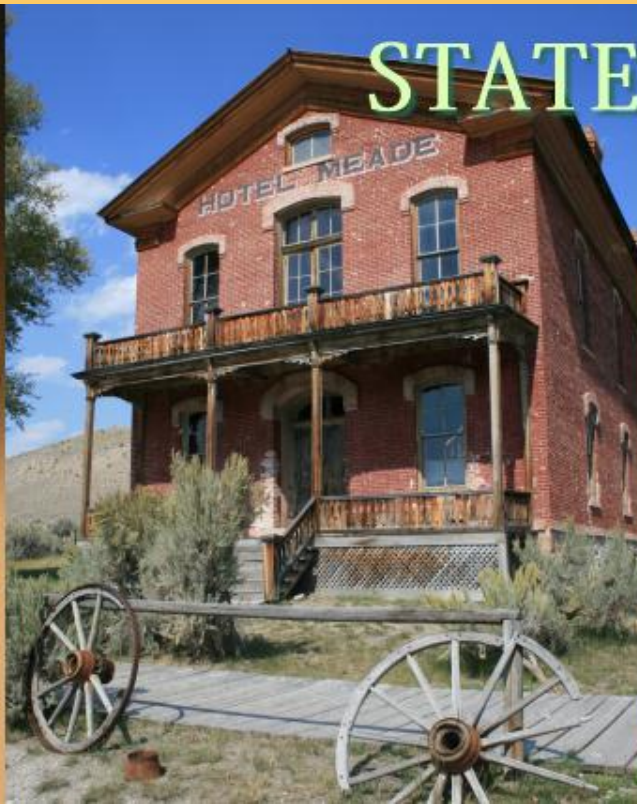
Timeline

- Deliberation through 2013 and observation of Pensions implementation
- Exposure drafts of both plan and employer reporting by April 2014
- Comment periods through July 2014
- Public hearings likely August 2014
- Redeliberation into 2015
- Final standards – June 2015
- Implementation – likely by July 1, 2016 for plans, July 1, 2017 for employers?

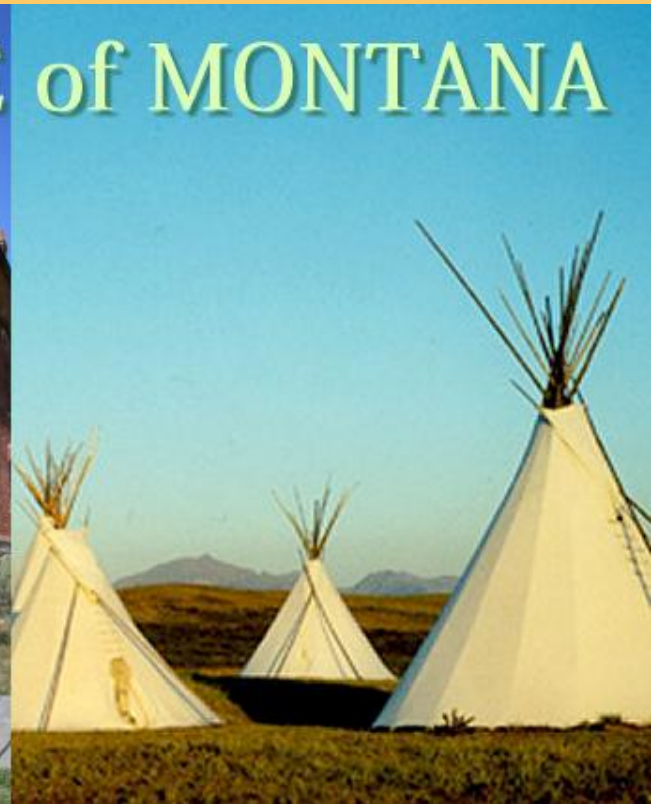
GAAP Hierarchy



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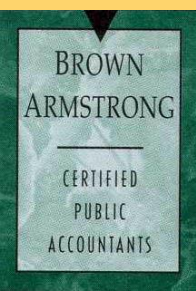


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GAAP Hierarchy Adjust

- KEY QUESTION
 - Should *Comprehensive Implementation Guide* be elevated to level 1 or 2 GAAP?
 - If so – full due process annually
 - BUT – many practitioners call it “GAAP.”
- Tentative Decisions
 - The GAAP hierarchy be reduced to **two levels of authoritative guidance and one level of nonauthoritative guidance**.
 - Compliance with GASB Concepts Statements prior to all other nonauthoritative literature should not be mandatory as this requirement would create a definitive hierarchy within the nonauthoritative literature.
 - Q&As in the *Guide* will be categorized as authoritative unless they only contain guidance that is directly stated in the related pronouncements or is illustrative.



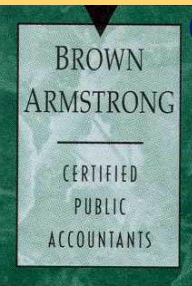
GAAP Hierarchy?

- Authoritative 1
 - GASB Standards
 - GASB Technical Bulletins
 - Authoritative Q&As from the *Implementation Guide*
- Authoritative 2
 - Other items from the *Implementation Guide*?
- Non-authoritative
 - GASB Concepts Statements
 - FASB ASCs
- Remaining Timeline –
 - ED in February 2014
 - Comment period through December 2014 (whole CIG needs to be commented on)
 - Final by June 2015



New Project on Leases

- Reexamination of all lease accounting due to pending FASB issuance of updated lease standards
- Key question – should capital and operating leases continue in current form?
 - FASB believes that the current lease model fails to represent the transactions faithfully as they omit relevant information about rights and obligations that meet the definition of assets and liabilities
 - Accounting and financial reporting is overly complex
- Result could be that all leases appear on statement of net position with annual reevaluation

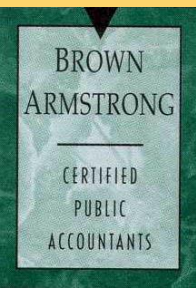


New Project on Leases

- FASB's view on Initial Measurement
 - Asset and liability recorded at commencement
 - Present value methodology (lessee's incremental borrowing rate)
 - Asset same as obligation (plus any recoverable initial direct costs)
 - Lease term defined as “longest possible term that is more likely than not to occur”
 - May require probability analysis for assessing renewal options.

New Project on Leases

- FASB's view on Subsequent Measurement
 - Asset amortized over useful life.
 - Interest expense recorded on obligation.
 - Reassess for changes in facts and circumstances.
- Other items of note
 - Lease incentives are not addressed yet
 - Certain leases outside the scope:
 - Intangible assets, mineral rights and biological assets.
 - Month to month leases would be in the scope of the lease term.



New Project on Leases – FASB Sample Calculation

Lease Term:	5 years		
Renewal Options:	two 2-year options		
Payments:	1,000 per mth		
	2nd 2 year	1st 2 year	No renewal
Lease term	9	7	5
Probablility	35%	45%	20%
Cumulative Probablility	35%	80%	100%
PV of Future Payments	\$68,453 (Based on incremental borrowing rate of 6%)		
Initial Measurement		DR	CR
Right-to-use asset	\$	68,453	
Lease Obligation			\$ 68,453
Subsequent Measurement			
Cash			\$ 1,000
Lease Obligation	\$	658	
Interest Expense	\$	342	
Depreciation Expense	\$	815	
Accumulated Depreciation			\$ 815

New Project on Leases

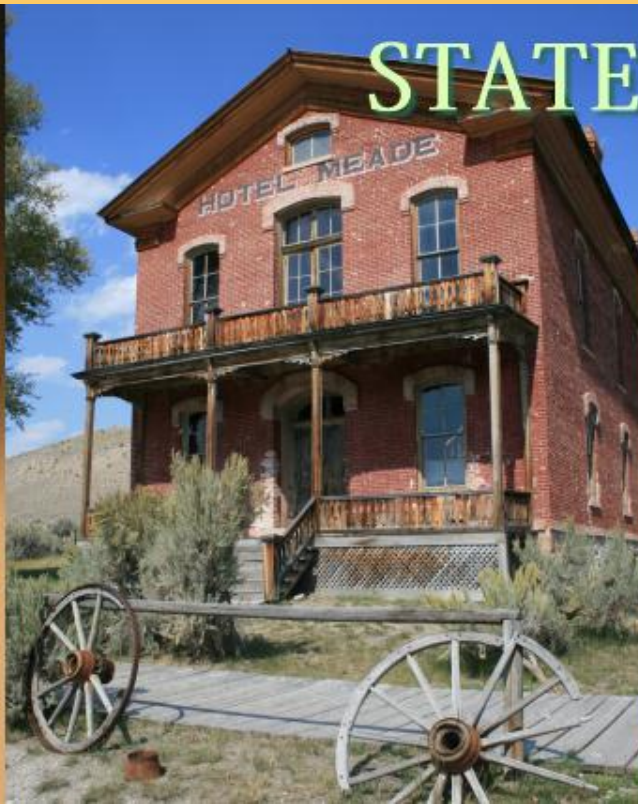
- Potential FASB Presentation:
 - Right to use asset reported in Capital Assets separate from other non-leased assets.
 - Amortization of right-to-use asset and interest expense on liability reported from other amortization separately, either on the financial statements or notes.
 - Cash payments on lease reported as financing activities in SCF (previously operating).



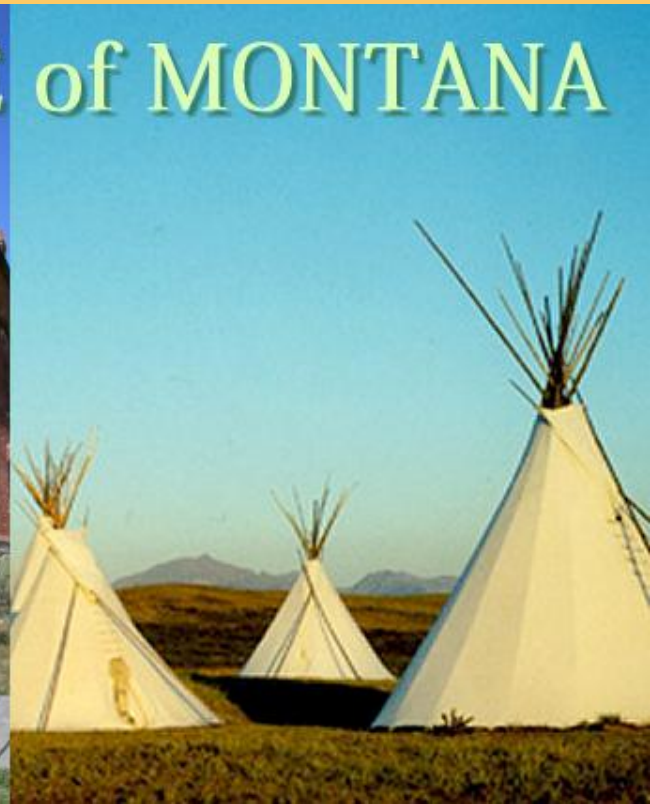
FAF Proposal on GASB's Scope of Authority



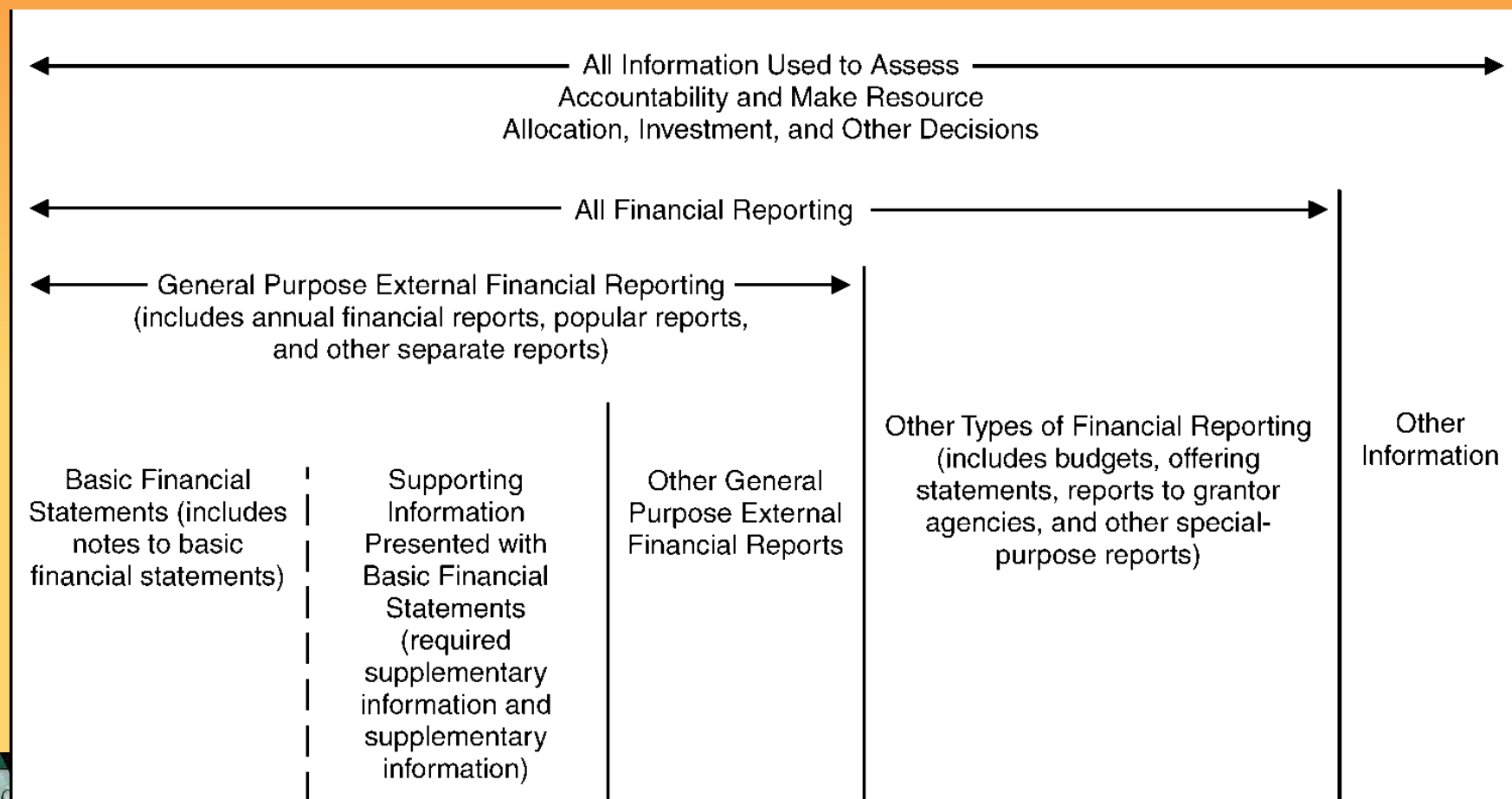
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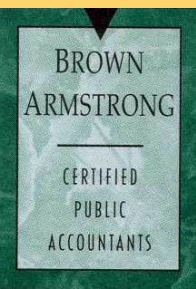


FAF Proposal—GASB Scope



FAF Proposal—Groups

- Group 1—Information clearly in scope
- Group 2—Information that the GASB believes is within its standard setting authority, but that is not clearly in Group 1
- Group 3—Clearly outside scope



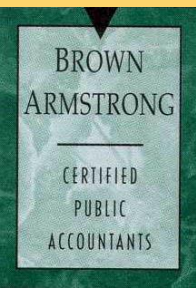
FAF Proposal—Enhanced Procedures for Group 2 Potential Projects

- Expanded project proposal
 - FAF Oversight Committee may conduct, or request that GASB conduct, additional constituent outreach
- FAF Oversight Committee will make a recommendation to the FAF Board of Trustees
- FAF Board of Trustees will decide if the project is within the GASB's scope
- After research phase is completed the FAF Oversight Committee may take additional action



FAF Proposal—Timetable

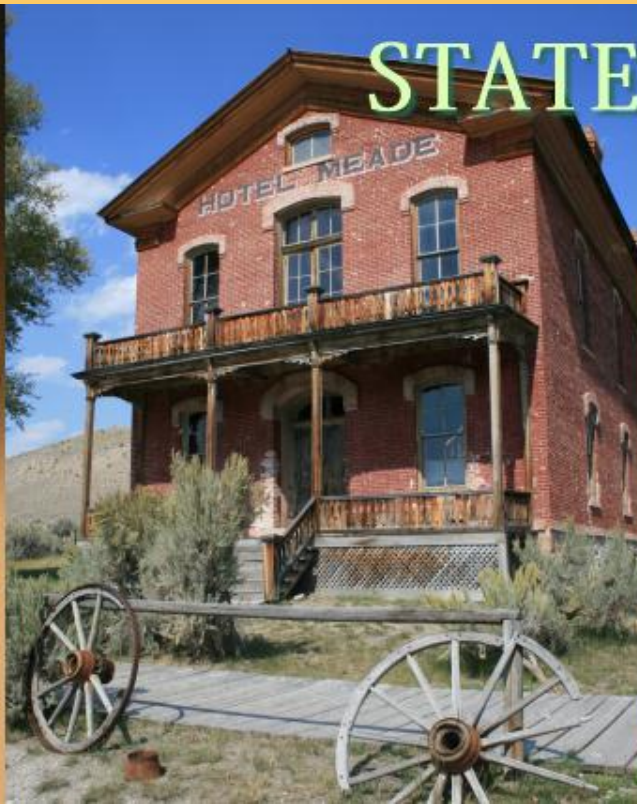
- Comments on the FAF Proposal requested by April 30, 2013



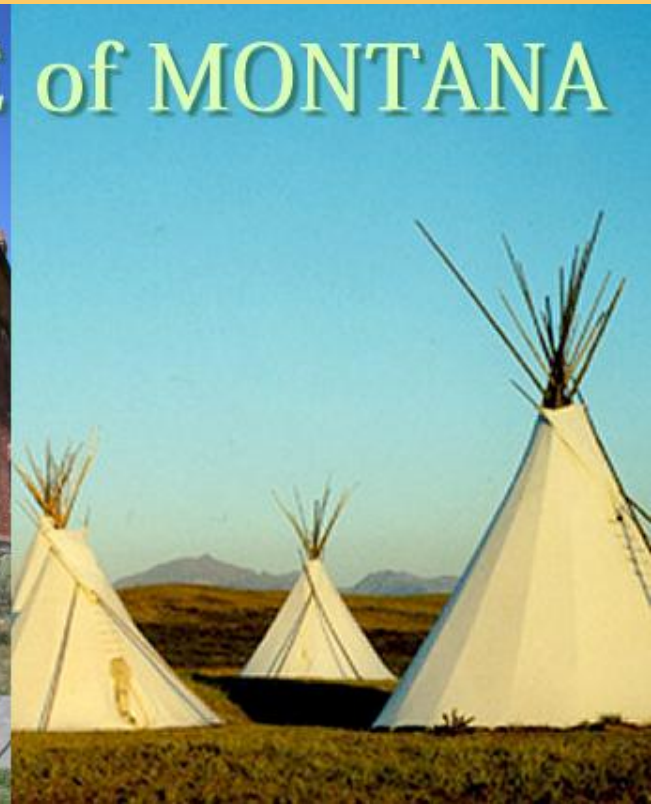
Auditing Update



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Agenda

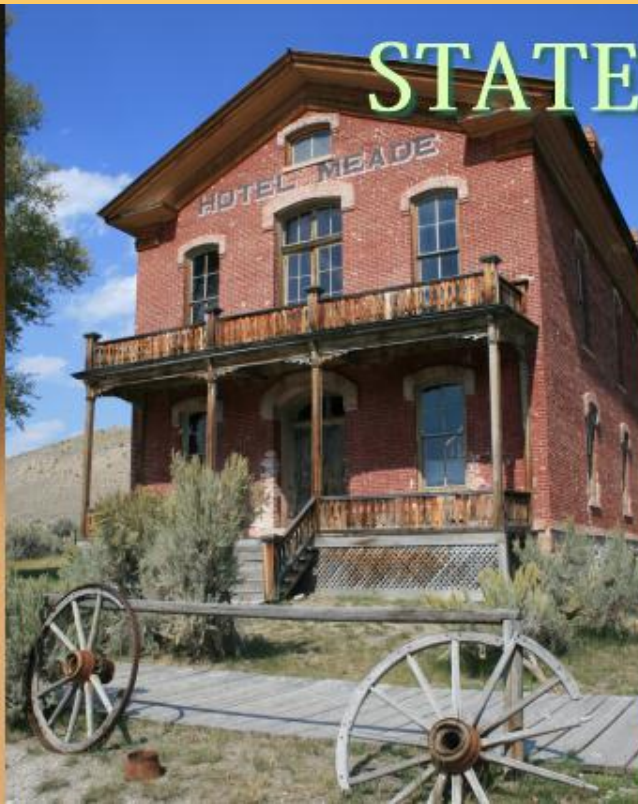
- Audit Update (Focus on Clarity Reports)
 - Other items – Group Audits, Special Purpose Frameworks (ex – OCBOA)
- Proposed Changes in Federal Audits
- Fraud? What Fraud? Ethics? What Ethics?



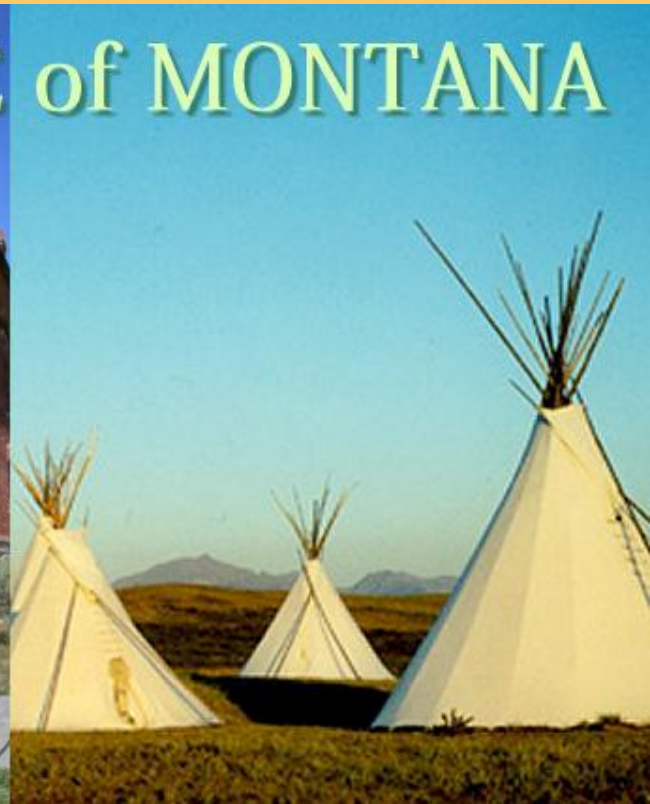
General Audit Update



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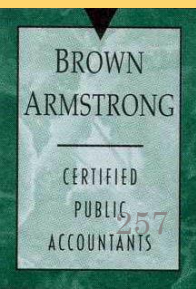


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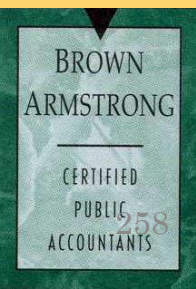
Major Changes that May have been Overlooked in Clarity Implementation

- Terminology Changes (AU-C section 200)
 - General, Field Work and Reporting Standards (10 General Standards) have been replaced
 - Training and proficiency, independence, due professional care
 - Supervision, Obtain an Understanding, Sufficient evidence
 - Reporting in accordance with GAAP, Consistent reporting, Adequate disclosure, Expression of an opinion
 - If an auditor fulfills the overall objective of the audit and meets applicable ethical requirements the ASB believes that the auditor will have fulfilled the requirements currently stated in the 10 standards



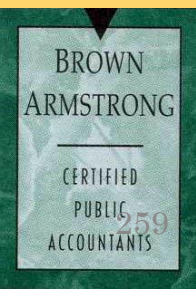
Overarching Changes with Clarity

- Terms of Engagement / Engagement Letters (AU-C section 210)
 - Requires the auditor to determine if preconditions for an audit are present
 - Acceptable **financial reporting framework** in the preparation and presentation of the financial statements and management acknowledgement of responsibility
 - The auditor is required to obtain the agreement of management that it:
 - acknowledges and understands its responsibility for selecting the appropriate financial reporting framework,
 - establishing and maintaining internal control, and
 - providing access and information to the auditor.
 - Auditor generally should not accept engagement with management-imposed scope limitation



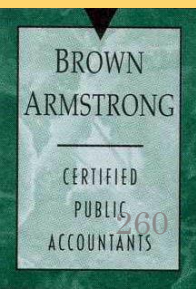
Overarching Changes With Clarity

- Considerations of Laws and Regulations - **important for Governments** (AU-C section 250)
 - requires the performance of procedures to identify instances of noncompliance with those laws and regulations that may have a material effect on the financial statements
- Opening Balances in Initial Audits (AU-C section 510)
 - Strengthens existing standards by making clear that reviewing a predecessor auditor's audit documentation cannot be the only procedure performed to obtain sufficient appropriate audit evidence regarding opening balances.
 - Bottom line – more work in transition audits!



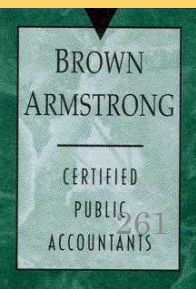
Overarching Changes With Clarity

- Group Audits (AU-C section 600)
 - Definitions
 - Responsibilities of the Group Engagement Partner
 - Making Reference
 - Involvement With, and Understanding of, Component Auditors
 - Materiality
 - Communication with Others and Documentation
- Using the Work of an Auditor's Specialist (AU-C 620)
 - Incremental documentation requirements for in-firm specialists (discussed yesterday)



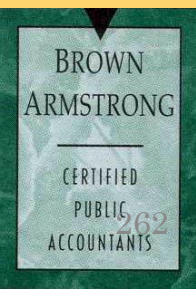
Overarching Changes With Clarity

- Forming an Opinion and Reporting on Financial Statements (AU-C 700) – **Totally changed reports**
 - Description of management's responsibility in more detail than AU section 508
 - Use of headings to clearly distinguish each section of the report
 - Report on the Financial Statements
 - Management's Responsibility for the F/S
 - More robust wording
 - Auditor's Responsibility
 - Opinion(s)
 - Other Matters
 - Report on Other Legal and Regulatory Requirements



Overarching Changes With Clarity(Reporting)

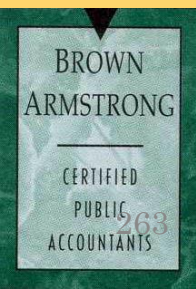
- Emphasis of Matter (AU-C section 706)
 - Refers to a matter appropriately presented or disclosed in the financial statements that, in the auditor's professional judgment, is of such importance that it is fundamental to users' understanding of the financial statements.
- Other Matter (AU-C section 706)
 - Refers to a matter other than those presented or disclosed in the financial statements that, in the auditor's professional judgment, is relevant to users' understanding of the audit, the auditor's responsibilities, or the auditor's report



Overarching Changes With Clarity (Reporting)

- Terminology Changes

Old Term	Clarified Term
Standard Report	Term not used because we refer to the opinion and not the report
Clean opinion/Qualified Opinion	Unmodified Opinion / Modified Opinion
Explanatory Paragraph	Emphasis-of-matter paragraph or other-matter paragraph (as applicable)
Explanatory Language	Additional communication

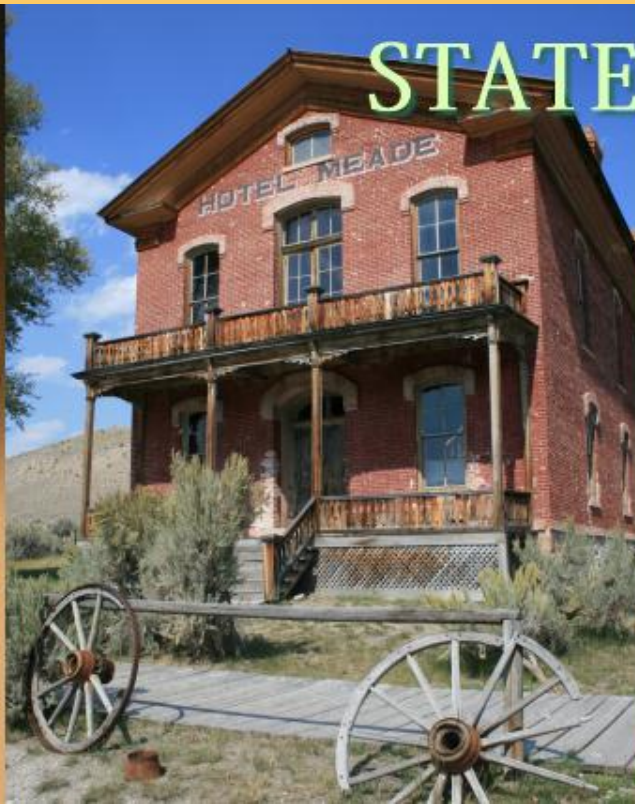




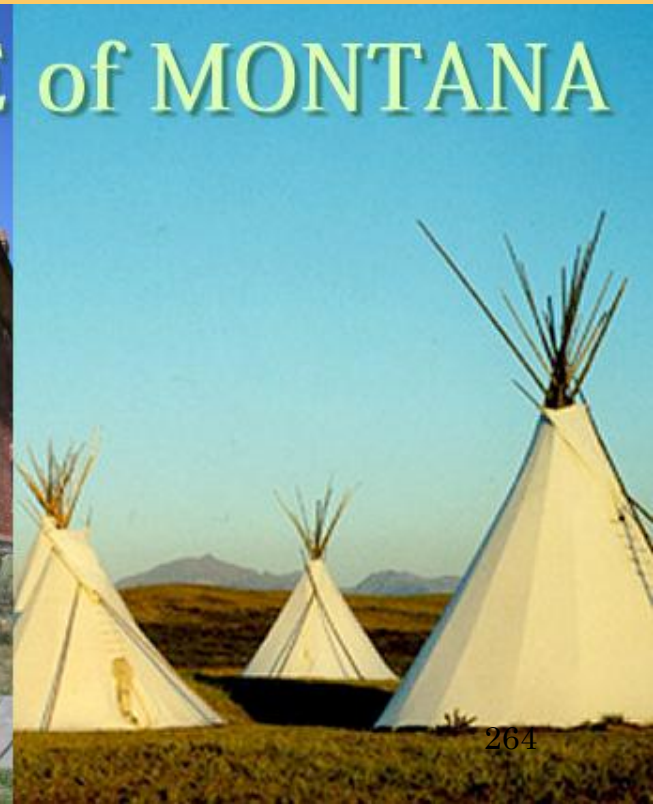
Group Audits



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How we got where we are— Group Audits

OLD / Superseded AICPA

- Make reference to work of others
- Divided responsibility

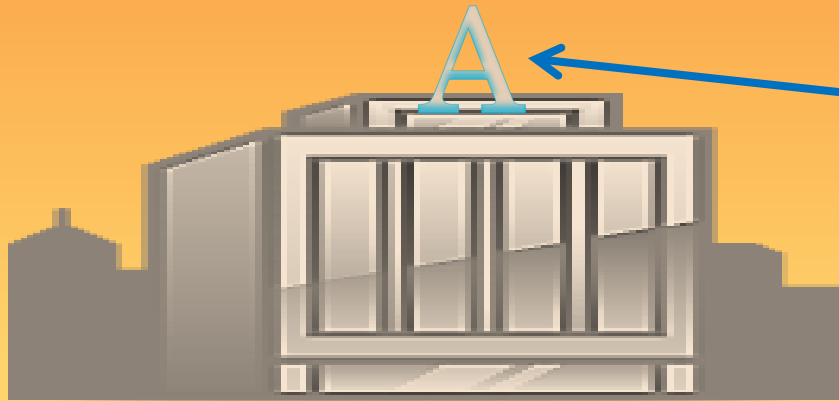
International Standards

- “Group” auditor has responsibility
- No making reference
- Group tells other auditors what to do

Clarified AICPA

- “Group” auditor has responsibility
- Making reference is basis for evidence
- Group assumes responsibility for components not referenced

So when do we have a group audit?

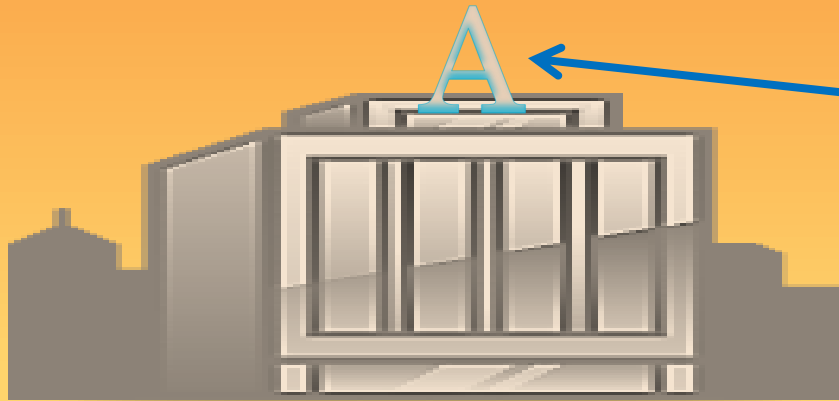


Entity A has its own operations



Entity B operated, managed, accounted for separately

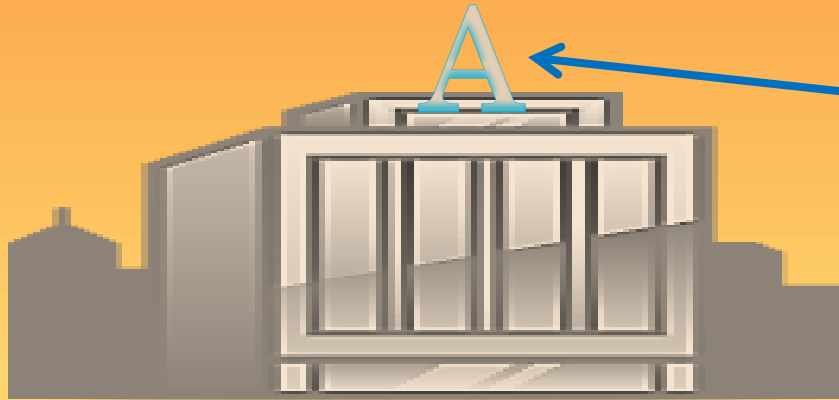
So when do we have a group audit?



Entity A
prepares F/S
that include
entity B's
financial
information



So when do we have a group audit?



Entity A is a group



Entity B is a component

Key definitions – Group examples


- *Group* – All the components whose financial information is included in the group financial statements
- *Group management* – Management responsible for the preparation of the group F/S
- *Group-wide controls* – Controls designed, implemented, and maintained by group management over group financial reporting

Key definitions – Component examples

- *Component* – An entity or activity for which group or component management prepares financial information that is required to be included in the group F/S
- *Component materiality* – Materiality for a component determined by the group engagement team for purposes of the group audit
- *Significant component* – Identified by the group engagement team i) of individual significance or ii) likely to include significant risks of material misstatement of the group F/S

Major sections of the standard

Acceptance and continuance - group auditor;
identify components; preconditions



Understanding - group; components;
component auditors; make reference?



Materiality decisions and responding to risks
of material misstatement

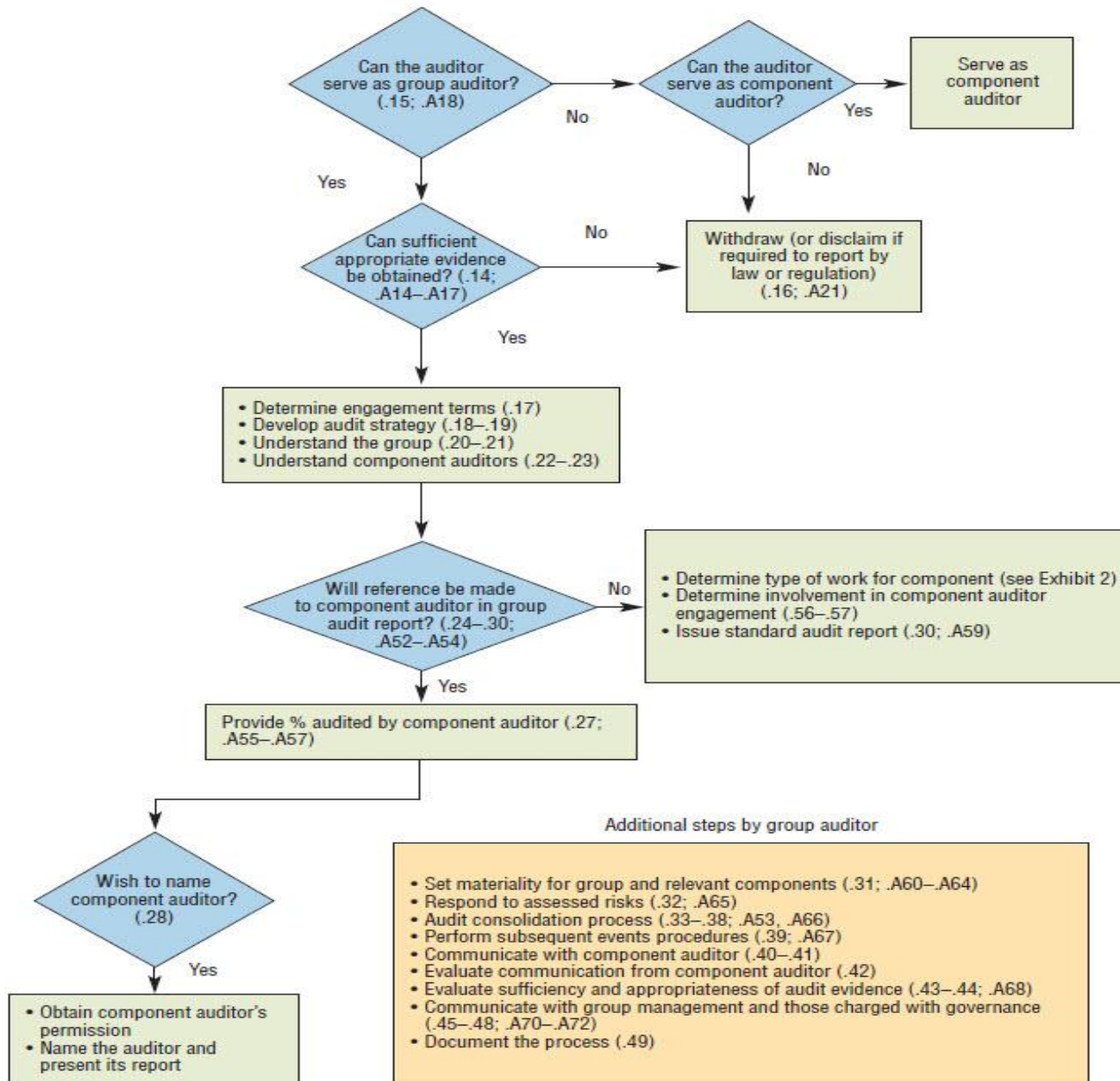


Other procedures - consolidation process;
subsequent events; evaluating evidence



Communications - with component auditors;
with group governance and management

Exhibit 1 The Group Audit Process*



*References are to paragraph numbers in AU-C 600.

How is an audit affected by Group Audits?

*During a
F/S Audit . .*

While you're at it . . .

Under-
stand the
Entity

- Identify components (§ .11)
- Understand components and consolidation process (§ .20)
- Decide which components are significant (§ .21)

Develop
Audit Plan

- Determine if significant components have component auditors and get an understanding (§ .22)
- Determine whether to/if you can make reference (§s .23-.25)

Determine
Materiality

- Determine component materiality for those components you are not making reference to and take into account components for which you are making reference (§ .31c)

How is an audit affected by Group Audits?

*During a
F/S Audit . .*

While you're at it . . .

Perform
procedures
to respond
to RMM

- Test consolidation processes (¶s .33-.38)
- When making reference, make communications to component auditor(s) (¶ .37, .40-.41)

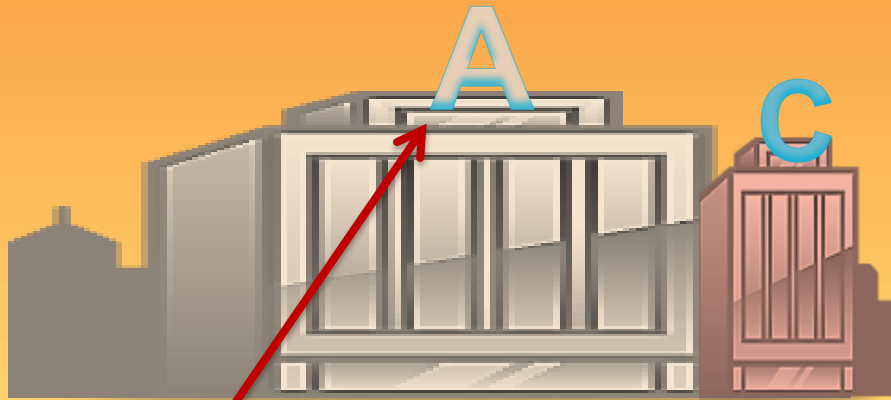
Evaluate
evidence

- Review communications and audit reports of component auditors you will be making reference to. (¶ .26, .42-.44)

By-the-way,
if you don't
make
reference

- Be involved in the component auditor(s) work (¶ .50-.64)
note: this involves a significant increase in the group auditor's procedures

Understanding a component is Critical!



Group – All the components whose financial information is included in the group financial statements. A group always has more than one component.

Component – An entity or activity for which group or component management prepares financial information that is required to be included in group financial statements.



Identifying components

Factors to Consider

- Legal structure
- Governance structure
- Management structure
- How decentralized financial reporting is
- Decentralized operations
- Control environment
- Nature of activity
- Uniqueness to entity
- Equity method investment
- Part of audit by other

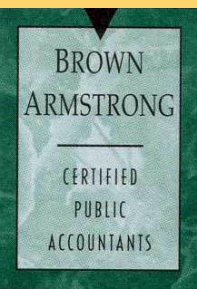
Other Indicators

- Physical location of assets
- Financial information prepared by others
- Existence of multiple general ledgers or records
- Whether information is booked in summary form
- If risk assessments vary
- Legal or regulatory requirements/oversight

Identifying components – Situation

#1

- A local government is preparing financial statements that needs to include a housing authority's financial information. The housing authority is a separate legal entity that has its own management, processes, financial system, and financial statement preparation. Is the housing authority a component of the local government?



Identifying components – Situation #2

- A local government is preparing financial statements that needs to include a hospital's financial information. The hospital is a separate line of business of the local government and has its own management, processes, financial system and financial statement preparation. Is the hospital a component of the local government?

Identifying components – Situation #3

- A local government is preparing financial statements that needs to include a landfill's financial information. The landfill is a separate line of business of the local government and has its own management, processes, financial system but does not prepare entity financial statements. Is the landfill a component of the local government?

Other considerations for governments

- Existence of components evaluated within individual opinion units
 - Each opinion unit usually its own (potential) group
 - Exception for other auditors of an opinion unit (a component)
- Departments within a major fund that are separately managed may also be components

Other considerations for governments

- For opinion units with multiple reporting units, components will commonly exist within:
 - Aggregate discretely presented component units
 - Individual component units whether audited by same audit firm or other auditors
 - Aggregate remaining fund information:
 - Pension or OPEB trust funds
 - Investment trust funds

Identifying components

Some “sure things” ???

- Need to make reference to the work of other auditors
- Investment accounted for under the equity method

Key questions to ask???

- My #1 – how does management prepare its financial statements; specifically, when do they have to incorporate financial information differently than from its own financial information system(s)?

Identifying components – practice issues

- Performance issues
 - Obtaining an understanding of the entity
 - Additional specific policies for criteria and factors?
 - Additional specific procedures for applying judgment and making determinations?

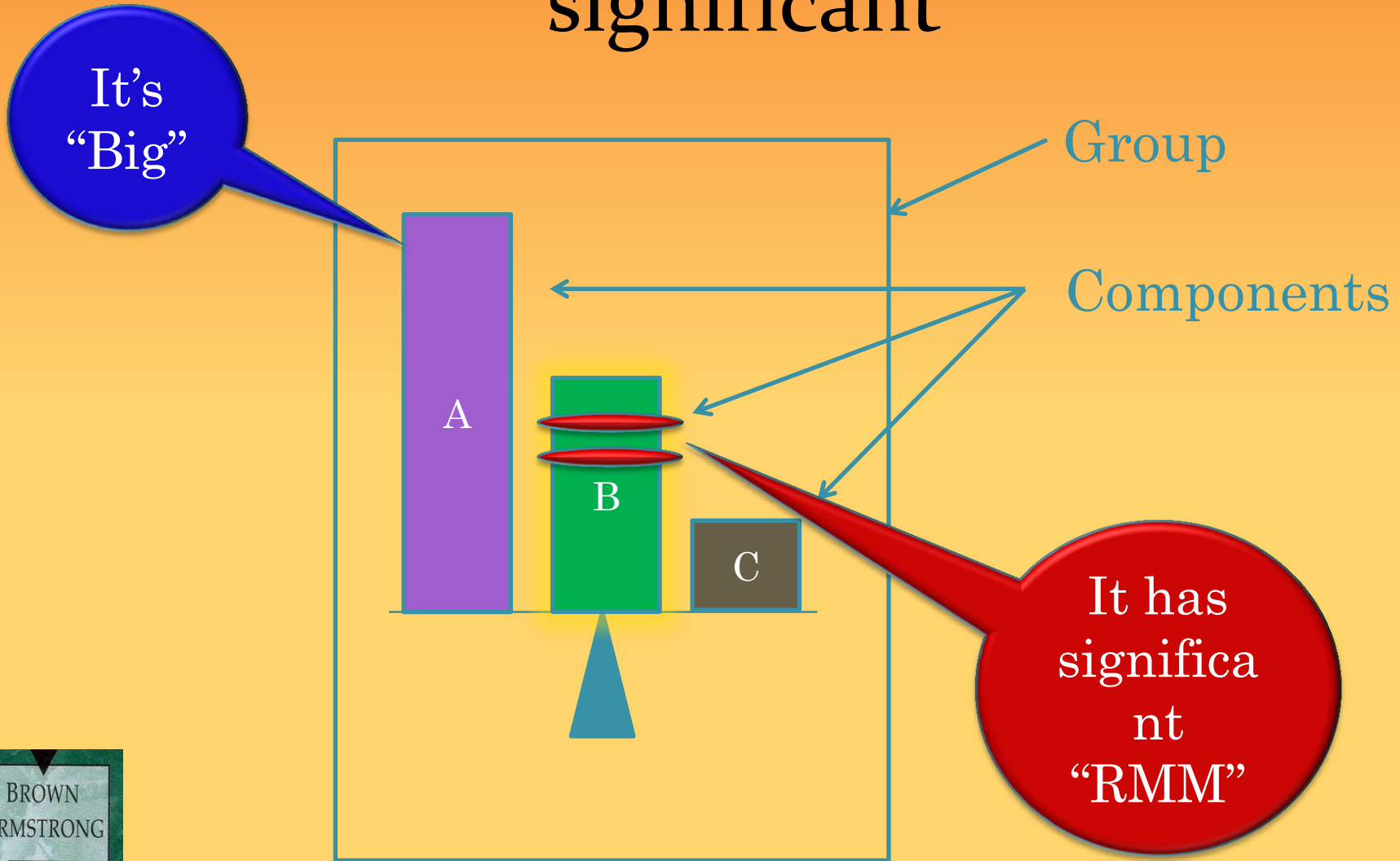
Identifying components – practice issues

- Documentation issues
 - Standard only requires (*related to identifying components*) . . .
 - Analysis of components indicating those that are significant and the type of work performed on component financial information
 - Those components for which reference is made
 - Additional documentation policies?
 - Spread across multiple areas or in one summary?

Special Considerations—Audit of Group Financial Statements (AU-C 600)

- Obtain an understanding of group, components and **group-wide controls**
- Obtain an understanding of the **consolidation process**
- Understanding sufficient to:
 - Confirm or revise initial identification of components likely to be significant
 - Assess RMM of group financial statements

Deciding what makes a component significant



Why do we care if components are significant?

Financially Significant Component

- Audit of financial information (adapted as necessary) using component materiality

Risk-based Significant Component

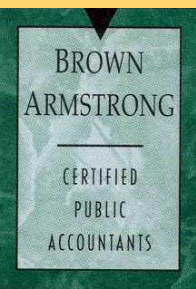
- Audit financial information (adapted as necessary) using component materiality
- Audit (adapted as necessary) of one or more class of transactions related to the risk
- Specific audit procedures designed to address the risk

Non-significant Components

- Analytical procedures to determine if significant risks of material misstatements
- If additional significant risks of material misstatements are identified, using auditor judgment, apply requirements of risk-based significant components

What if there are component auditors?

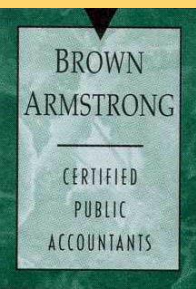
- Obtain an understanding of the component auditor (whether or not group auditor will make reference)
 - Whether a Component Auditor (CA) will comply with ethical requirements, especially independence
 - About the CA's professional competence
 - The extent, if any, the GA will be able to be involved in the CA's work
 - Whether the GA will be able to obtain information affecting the consolidation process
 - Whether a CA operates in a regulatory environment that oversees auditors



What if there are component auditors?

- Preconditions to making reference to others' work
 - Component auditor followed GAAS (or the relevant requirements of GAAS*)
 - Component auditor report is not restricted as to use (remember GAGAS exception)

* Requires additional documentation



What if there are component auditors?

- Preconditions to making reference to others' work
 - Component f/s prepared on same financial reporting framework*
 - Unless criteria for all material items are similar to criteria for those in group f/s; and group auditor evaluates appropriateness of conversion adjustments**
- * Exception in application paragraphs for GASB and FASAB, which address this
- ** Requires additional reporting

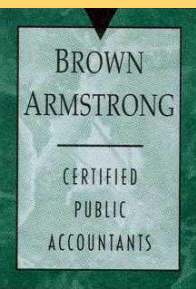


Here's the pink elephant sitting in the room we may have ignored in the past:

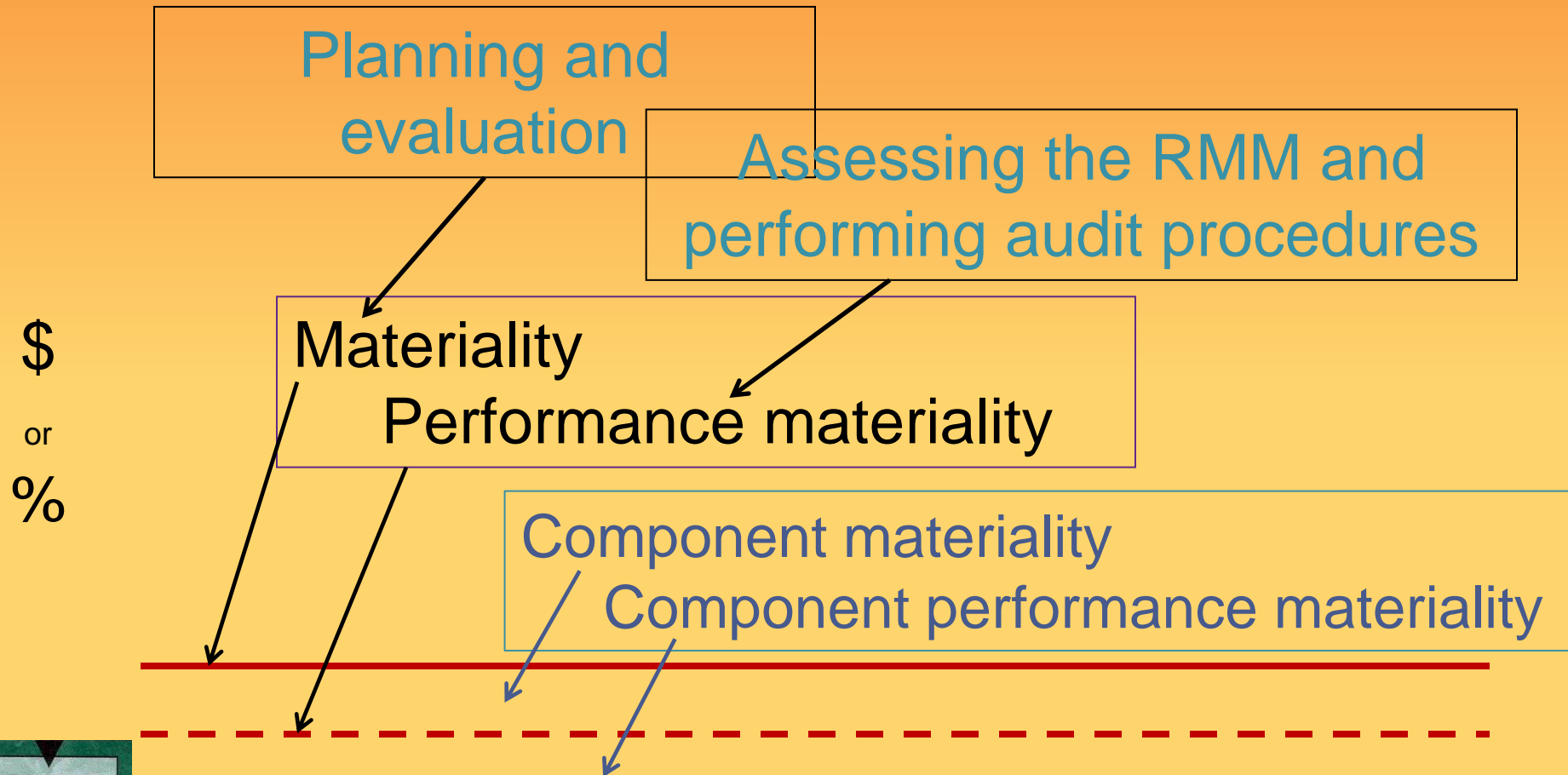
When a component auditor does not meet the independence requirements relevant to the group audit or the group auditor has serious concerns about the CA (the other matters listed in the previous slide), the group auditor should obtain sufficient appropriate audit evidence relating to the financial information of the component without making reference to the audit of that component auditor in the auditor's report on the group financial statements or otherwise using the work of that component auditor.

Special Considerations—Audit of Group Financial Statements (AU-C 600)

- Materiality – the GA should determine:
 - Materiality, incl. performance materiality, for group financial statements
 - Whether specific circumstances exist for which something less than materiality would influence users; if so, apply a different materiality to those transactions, balances, or disclosures
 - Component materiality for components that will be audited – component materiality s/b lower than group materiality and component performance materiality s/b lower than group performance materiality
 - Threshold below which misstatements are trivial



Materiality in Planning and Performing an Audit (AU-C 320)



Special Considerations—Audit of Group Financial Statements (AU-C 600)

Practice Issues:

Group-wide controls & Consolidation Process

- Test group-wide controls – but who – GA or CA?
- Test consolidation process – but who – GA or CA?

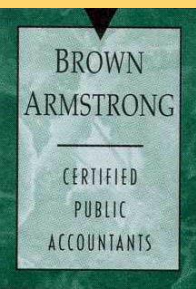
Subsequent events (SE) issues:

- How often does component audit work finish before group audit team is done?
- Who is responsible for SE work – GA or CA?

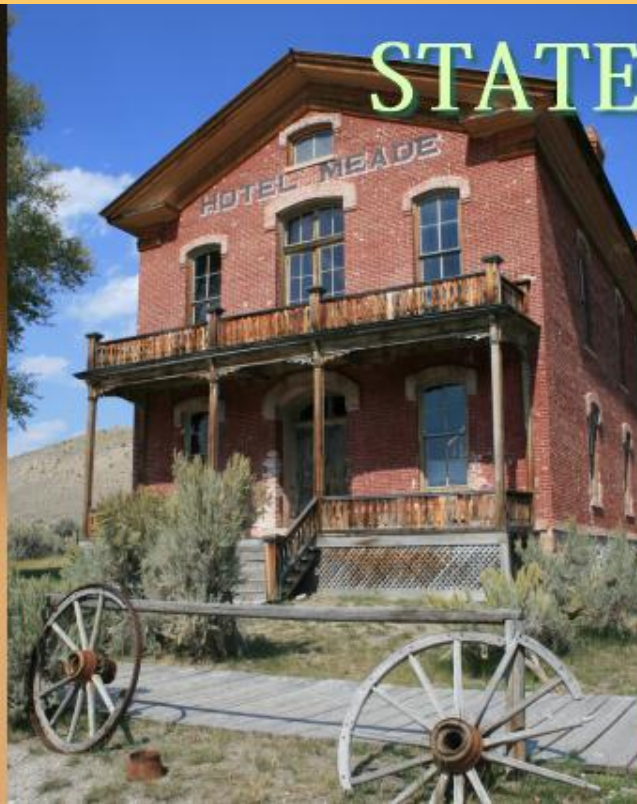
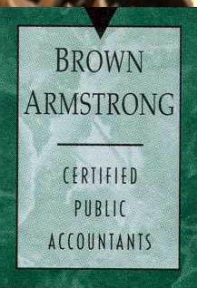
Special Considerations—Audit of Group Financial Statements (AU-C 600)

Final thought:

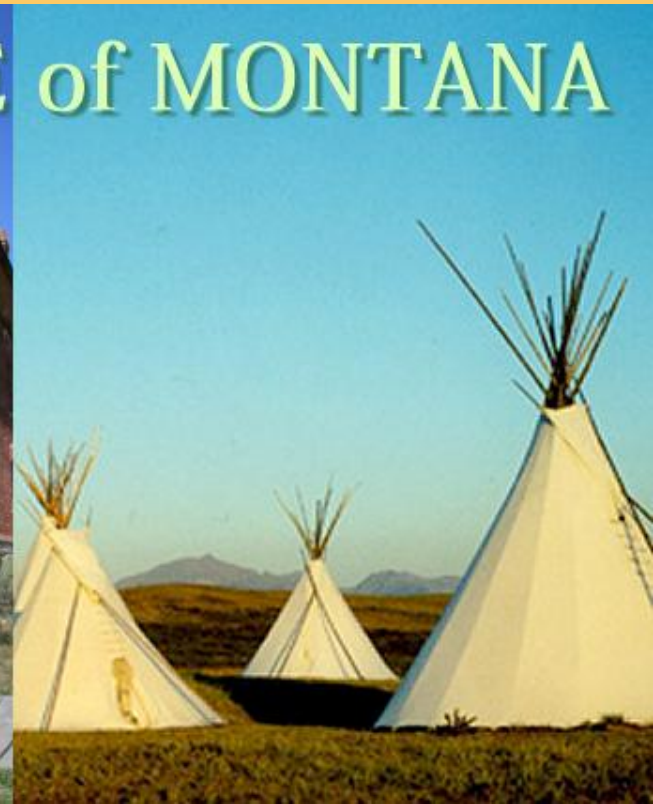
- The requirements for a group auditor who does not make reference to a component auditor's report, and decides instead to take responsibility for the work of a component auditor has a **SIGNIFICANT** increase in requirements compared to:
 - Current guidance on the matter
 - When making reference under this new AU section



Special Purpose Frameworks (used to be OCBOA)



STATE of MONTANA

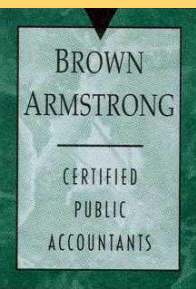


Special Considerations—Special Purpose Frameworks (AU-C 800)

- Replaces OCBOA with cash, tax, contractual and regulatory / legislative
 - Then SAS 127 modified it
- Requires the auditor to understand the purpose and intended users for framework appropriateness
- Audit still based on the rest of GAAS, but this section provides the reporting requirements and guidance

Special Purpose Frameworks

- **Special purpose financial statements.** Financial statements prepared in accordance with a special purpose framework.
- **Special purpose framework.** A financial reporting framework other than GAAP that is one of the following bases of accounting
 - **Regulatory basis.** A basis of accounting that the entity uses to **comply with the requirements or financial reporting provisions of a regulatory agency** to whose jurisdiction the entity is subject (for example, a basis of accounting that insurance companies use pursuant to the accounting practices prescribed or permitted by a state insurance commission or state-specific GAAP).
 - **Other basis.** A basis of accounting that uses a definite set of logical, reasonable criteria that is applied to all material items appearing in financial statements.



Disclosures Must Include

- Description of the special purpose framework, including a summary of significant accounting policies, and how the framework differs from GAAP, the effects of which need not be quantified.
- Informative disclosures similar to those required by GAAP, in the case of special purpose financial statements that contain items that are the same as, or similar to, those in financial statements prepared in accordance with GAAP.
- A description of any significant interpretations of the contract on which the special purpose financial statements are based, in the case of special purpose financial statements prepared in accordance with a contractual basis of accounting.
- Additional disclosures beyond those specifically required by the framework that may be necessary for the special purpose financial statements to achieve fair presentation



Special Considerations—Special Purpose Frameworks (AU-C 800)

	Cash Basis	Tax Basis	NEW! Other basis	Contractual	Regulatory	
					Restricted	General
Opinion	Single	Single	Single	Single	Single	Dual
Describe Purpose	No	No	No	Yes	Yes	Yes
Use EOM?	Yes	Yes	Yes	Yes	Yes	No
Restrict use?	No	No	Yes	Yes	Yes	No

Special Purpose Reports

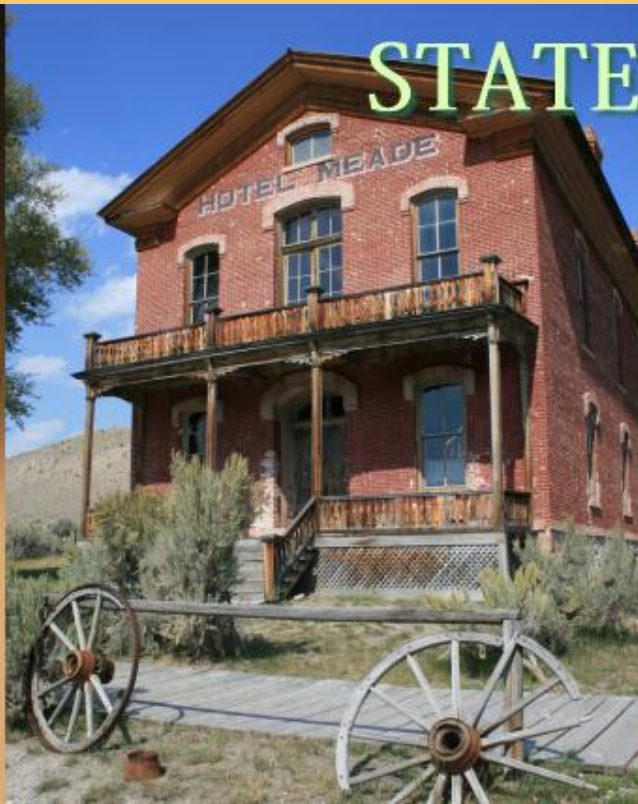
- Report by definition is modified
 - Report includes reference to definition of framework
 - Financial reports must be suitably titled
 - Key question – are the financial reports fairly stated?
- If reporting on less than an entire government – emphasis of a matter
- BUT – if report is for general use (not restricted) then **adverse opinion**



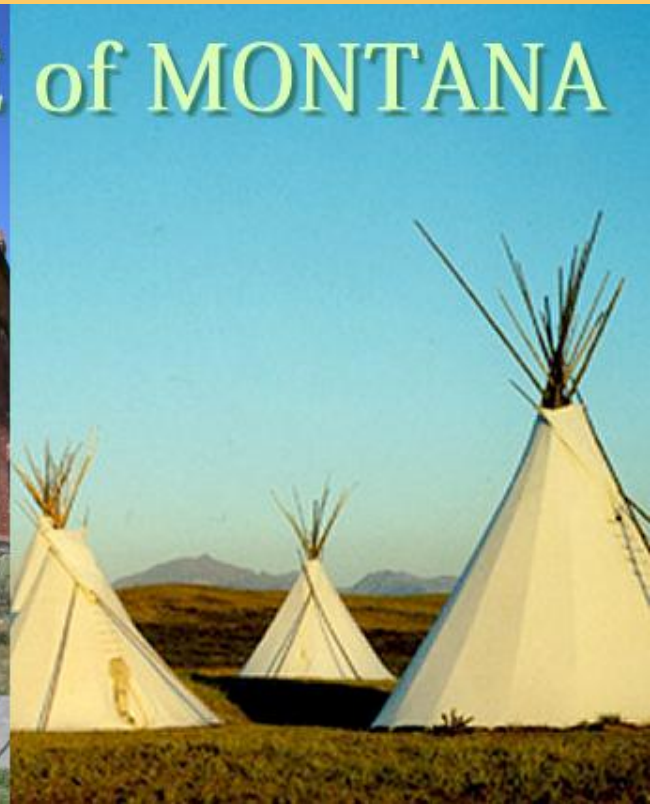
Clarity Reports for Governments



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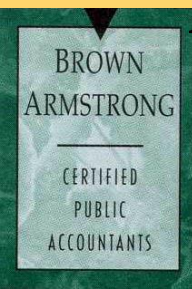
Unmodified Report –variations in general release so far

Independent Auditor's Report

[*Appropriate Addressee*]

Report on the Financial Statements

We have audited the accompanying financial statements of the governmental activities, the business-type activities, the aggregate discretely presented component units, each major fund, and the aggregate remaining fund information of the City of Example, Any State, as of and for the year ended June 30, 20X1, and the related notes to the financial statements, which collectively comprise the City's basic financial statements as listed in the table of contents.



STATE of MONTANA

Unmodified Report – variations in general release so far

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Unmodified Report – variations in general release so far

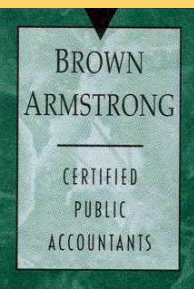
Auditor's Responsibility

Our responsibility is to express opinions on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinions

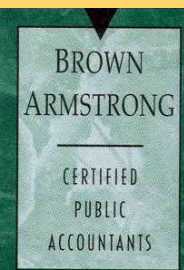


STATE of MONTANA

Unmodified Report – variations in general release so far

Opinions

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, the business-type activities, the aggregate discretely presented component units, each major fund, and the aggregate remaining fund information of the City of Example, Any State, as of June 30, 20X1, and the respective changes in financial position, and, where applicable, cash flows thereof for the year then ended in accordance with accounting principles generally accepted in the United States of America.

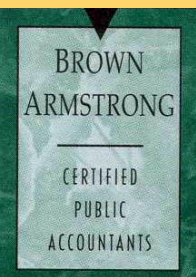


Unmodified Report – variations in general release so far

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the [*identify required supplementary information, such as management's discussion and analysis and budgetary comparison information*] on pages XX–XX and XX–XX be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.



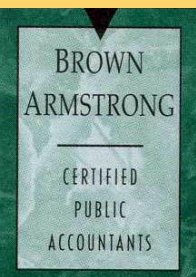
STATE of MONTANA

Unmodified Report – variations in general release so far

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the [*identify required supplementary information, such as management's discussion and analysis and budgetary comparison information*] on pages XX–XX and XX–XX be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

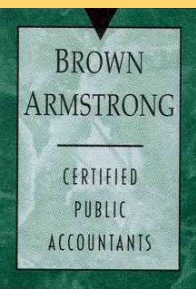


Unmodified Report – variations in general release so far

Other Information

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the City of Example's basic financial statements. The [*identify accompanying supplementary information, such as the combining and individual nonmajor fund financial statements, and the other information, such as the introductory and statistical sections*] are presented for purposes of additional analysis and are not a required part of the basic financial statements.

The [*identify accompanying supplementary information*] is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the basic financial statements or to the basic financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the [*identify accompanying supplementary information*] is fairly stated, in all material respects, in relation to the basic financial statements as a whole.



STATE of MONTANA

Unmodified Report – variations in general release so far

The [*identify the other information*] has not been subjected to the auditing procedures applied in the audit of the basic financial statements, and accordingly, we do not express an opinion or provide any assurance on it.

Report on Other Legal and Regulatory Requirements

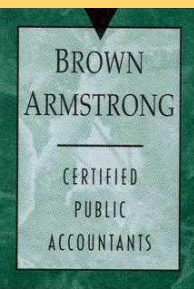
[*Form and content of this section of the auditor's report will vary depending on the nature of the auditor's other reporting responsibilities, if any.*]

[*Auditor's signature*]

[*Auditor's city and state*]

[*Date of the auditor's report*]

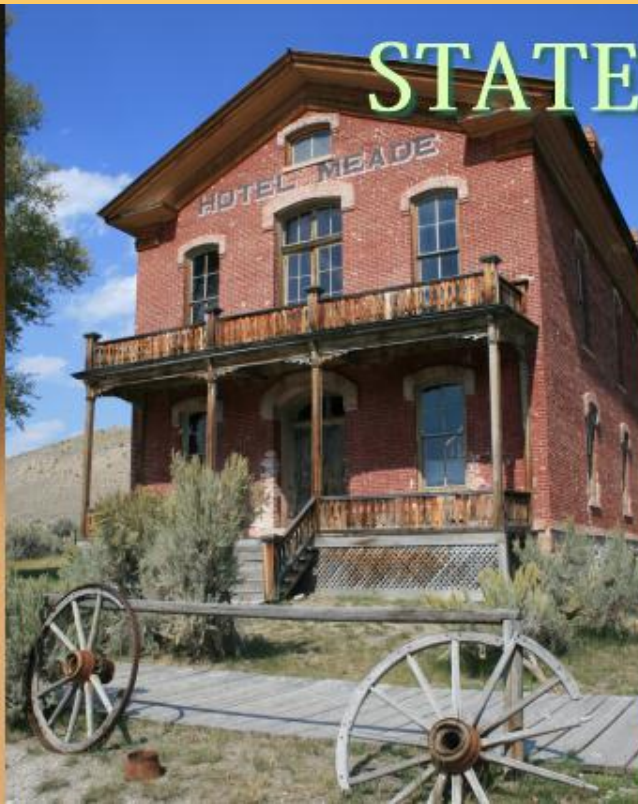
Additional variations for modified reports, fund only reports, single opinion units.



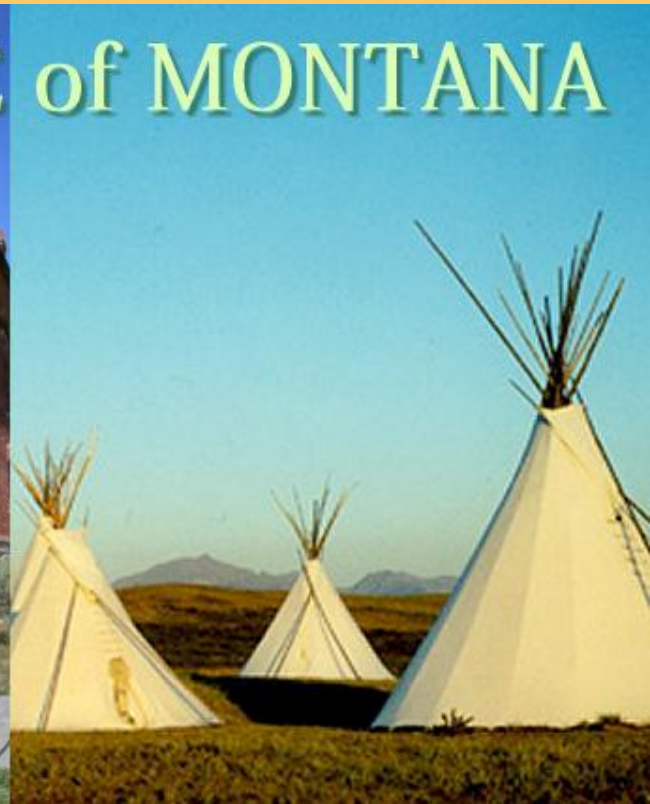
GAGAS Reports



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GAGAS Reports

Independent Auditor's Report

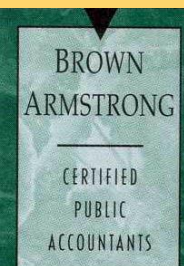
[Appropriate Addressee]

Report on the Financial Statements

We have audited the accompanying financial statements of the governmental activities, the business-type activities, the aggregate discretely presented component units, each major fund, and the aggregate remaining fund information of the City of Example, Any State, as of and for the year ended June 30, 20X1, and the related notes to the financial statements, which collectively comprise the City's basic financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.



STATE of MONTANA

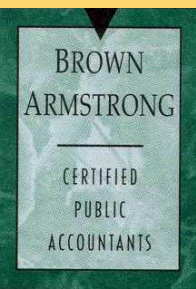
GAGAS Reports

Auditor's Responsibility

Our responsibility is to express opinions on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinions.

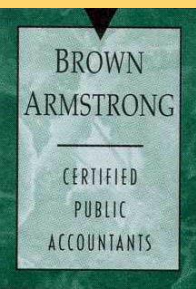


GAGAS Reports

Opinions

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, the business-type activities, the aggregate discretely presented component units, each major fund, and the aggregate remaining fund information of the City of Example, Any State, as of June 30, 20X1, and the respective changes in financial position and, where applicable, cash flows thereof for the year then ended in accordance with accounting principles generally accepted in the United States of America.

RSI / OI the same



STATE of MONTANA

GAGAS Reports

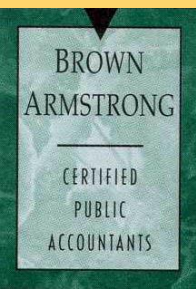
Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated [*date of report*] on our consideration of the City of Example's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering City of Example's internal control over financial reporting and compliance.

[*Auditor's signature*]

[*Auditor's city and state*]

[*Date of the auditor's report*]



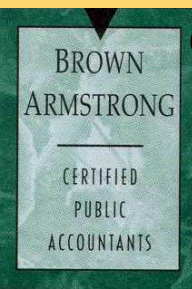
STATE of MONTANA

Internal Control Reports - Unmodified

Independent Auditor's Report

[Appropriate Addressee]

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of the governmental activities, the business-type activities, the aggregate discretely presented component units, each major fund, and the aggregate remaining fund information of Example Entity, as of and for the year ended June 30, 20X1, and the related notes to the financial statements, which collectively comprise Example Entity's basic financial statements, and have issued our report thereon dated August 15, 20X1.



STATE of MONTANA

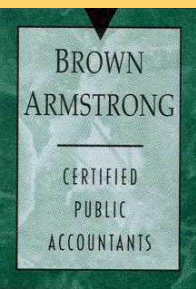
Internal Control Reports - Unmodified

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered Example Entity's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of Example Entity's internal control. Accordingly, we do not express an opinion on the effectiveness of Example Entity's internal control.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.



Internal Control Reports - Unmodified

Compliance and Other Matters

As part of obtaining reasonable assurance about whether Example Entity's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

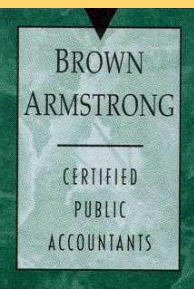
Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the entity's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

[Auditor's signature]

[Auditor's city and state]

[Date of the auditor's report]

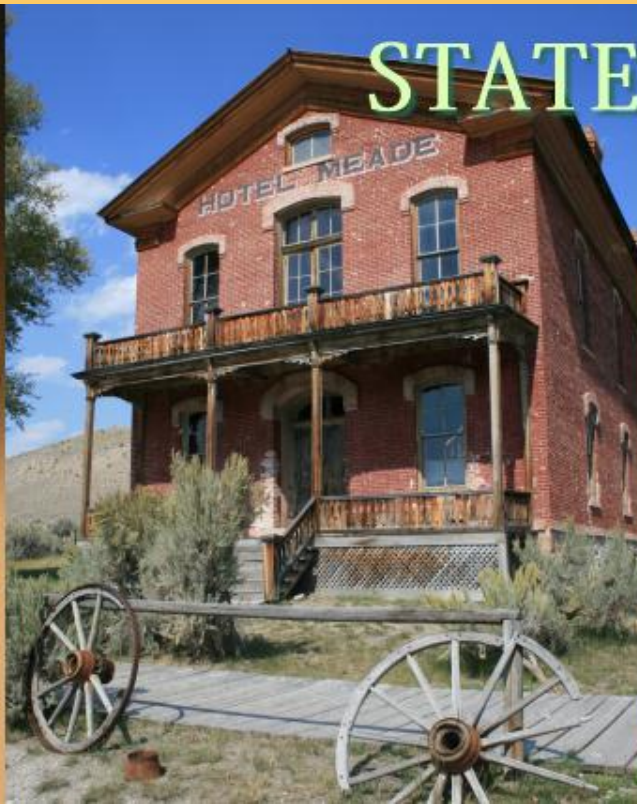


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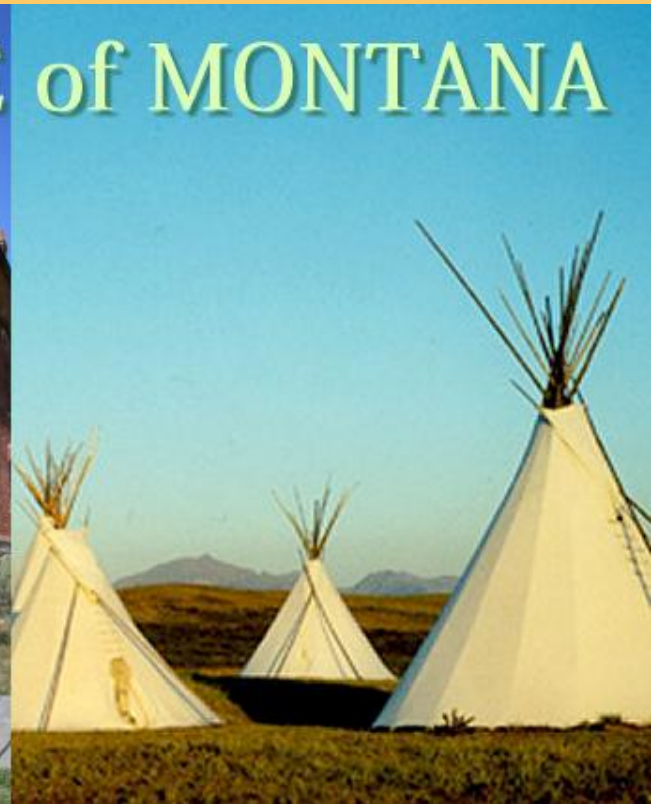
A-133 Reports



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A-133 Reports

Independent Auditor's Report

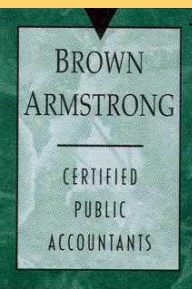
[*Appropriate Addressee*]

Report on Compliance for Each Major Federal Program

We have audited Example Entity's compliance with the types of compliance requirements described in the *OMB Circular A-133 Compliance Supplement* that could have a direct and material effect on each of Example Entity's major federal programs for the year ended June 30, 20X1. Example Entity's major federal programs are identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs.

Management's Responsibility

Management is responsible for compliance with the requirements of laws, regulations, contracts, and grants applicable to its federal programs.



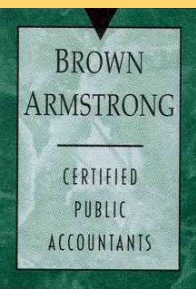
STATE of MONTANA

A-133 Reports

Auditor's Responsibility

Our responsibility is to express an opinion on compliance for each of Example Entity's major federal programs based on our audit of the types of compliance requirements referred to above. We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about Example Entity's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances.

We believe that our audit provides a reasonable basis for our opinion on compliance for each major federal program. However, our audit does not provide a legal determination of Example Entity's compliance.



A-133 Reports

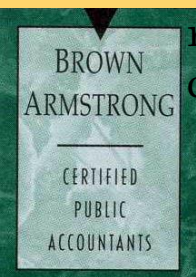
Opinion on Each Major Federal Program

In our opinion, Example Entity complied, in all material respects, with the types of compliance requirements referred to above that could have a direct and material effect on each of its major federal programs for the year ended June 30, 20X1.

Other Matters

The results of our auditing procedures disclosed instances of noncompliance, which are required to be reported in accordance with OMB Circular A-133 and which are described in the accompanying schedule of findings and questioned costs as items [*list the reference numbers of the related findings, for example, 20X1-1 and 20X1-2*]. Our opinion on each major federal program is not modified with respect to these matters.

Example Entity's response to the noncompliance findings identified in our audit are described in the accompanying [*insert name of document containing management's response to the auditor's findings; for example, schedule of findings and questioned costs and/or corrective action plan*]. Example Entity's response was not subjected to the auditing procedures applied in the audit of compliance and, accordingly, we express no opinion on the response.

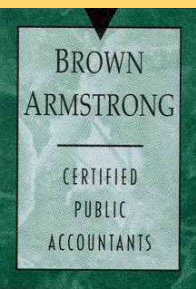


A-133 Reports

Report on Internal Control Over Compliance

Management of Example Entity is responsible for establishing and maintaining effective internal control over compliance with the types of compliance requirements referred to above. In planning and performing our audit of compliance, we considered Example Entity's internal control over compliance with the types of requirements that could have a direct and material effect on each major federal program to determine the auditing procedures that are appropriate in the circumstances for the purpose of expressing an opinion on compliance for each major federal program and to test and report on internal control over compliance in accordance with OMB Circular A-133, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of Example Entity's internal control over compliance.

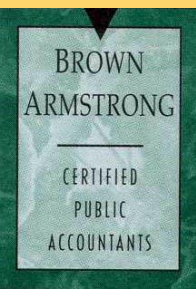
A *deficiency in internal control over compliance* exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance with a type of compliance requirement of a federal program on a timely basis. A *material weakness in internal control over compliance* is a deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected, on a timely basis.



A-133 Reports

A *significant deficiency in internal control over compliance* is a deficiency, or a combination of deficiencies, in internal control over compliance with a type of compliance requirement of a federal program that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance. Our consideration of internal control over compliance was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over compliance that might be material weaknesses or significant deficiencies. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

The purpose of this report on internal control over compliance is solely to describe the scope of our testing of internal control over compliance and the results of that testing based on the requirements of OMB Circular A-133. Accordingly, this report is not suitable for any other purpose.



A-133 Reports

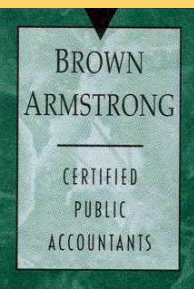
Report on Schedule of Expenditures of Federal Awards Required by OMB Circular A-133

We have audited the financial statements of Example Entity as of and for the year ended June 30, 20X1, and have issued our report thereon dated August 15, 20X1, which contained an unmodified opinion on those financial statements. Our audit was conducted for the purpose of forming an opinion on the financial statements as a whole. The accompanying schedule of expenditures of federal awards is presented for purposes of additional analysis as required by OMB Circular A-133 and is not a required part of the financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the schedule of expenditure of federal awards is fairly stated in all material respects in relation to the financial statements as a whole.

[Auditor's signature]

[Auditor's city and state]

[Date of the auditor's report]

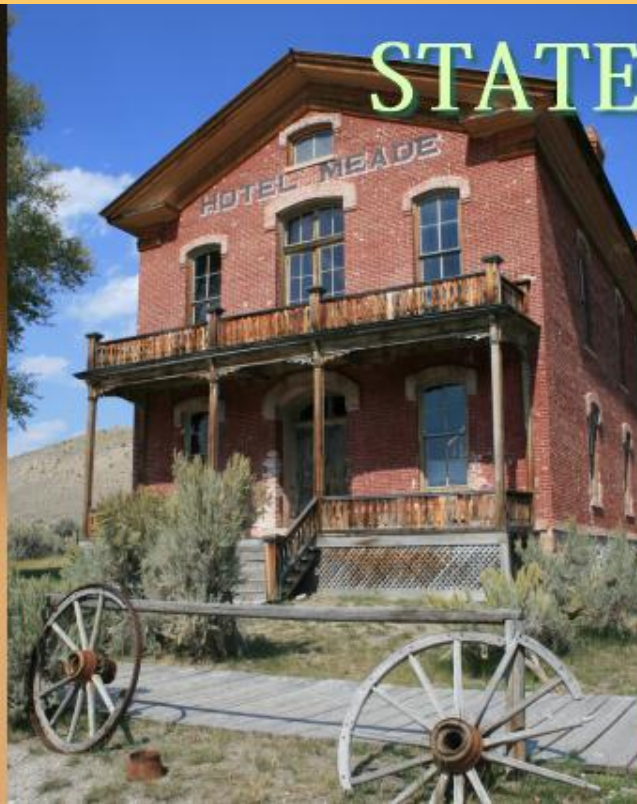


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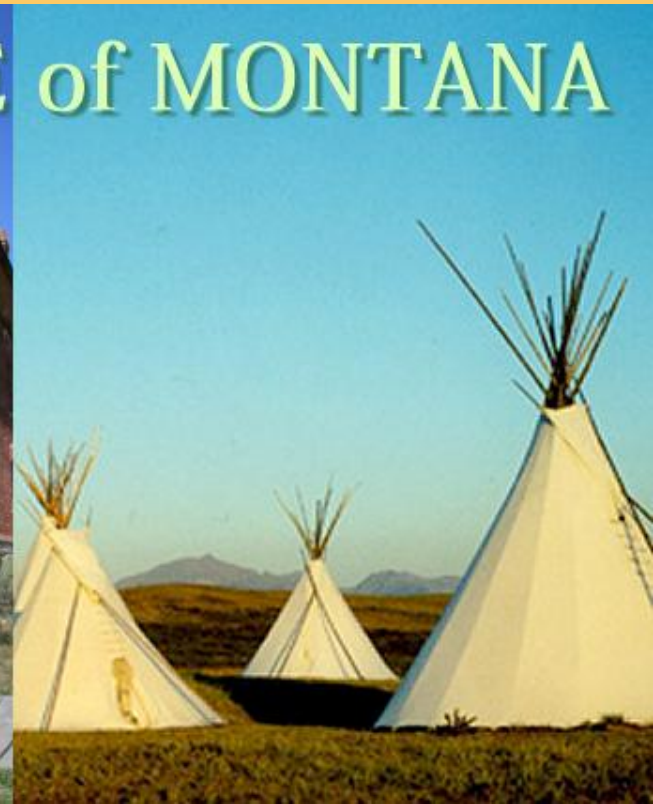
HUD Report /Audit Changes



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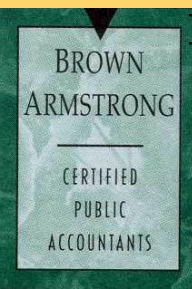
HUD changes

- Chapter 2 of HUD Audit Guide finally updated
 - Reformats the reporting structure
 - Aligns HUD's reporting guidance with the 2011 *Government Auditing Standards* and GAAS
 - HUD is suggesting one report to meet the requirements of *Government Auditing Standards* and a separate report that provides an opinion on compliance for each major HUD program and the related reporting on internal control over compliance.



Key Changes - HUD

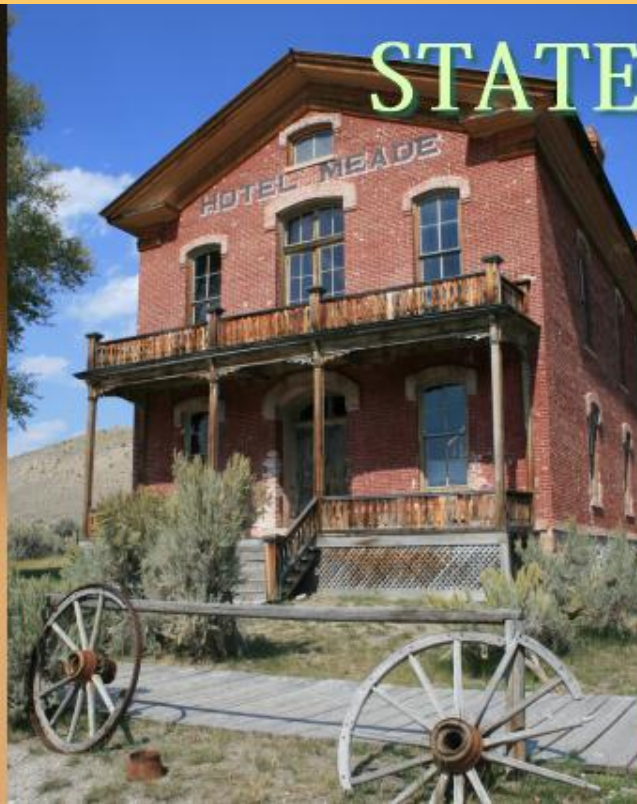
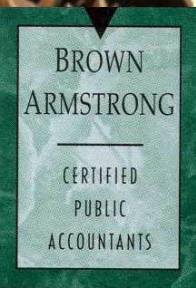
- Revised wording in all reports to adhere to new requirements in both the clarity auditing standards and *Government Auditing Standards*;
- In the financial statement report, the addition of various subheadings describing the financial statement audit including "Management's Responsibility," the "Auditor's Responsibility," and "Other Matters" (e.g., reporting on other information or required supplementary information);
- In the financial statement report, the addition of a new subheading describing the linkage to the reporting required by *Government Auditing Standards*;



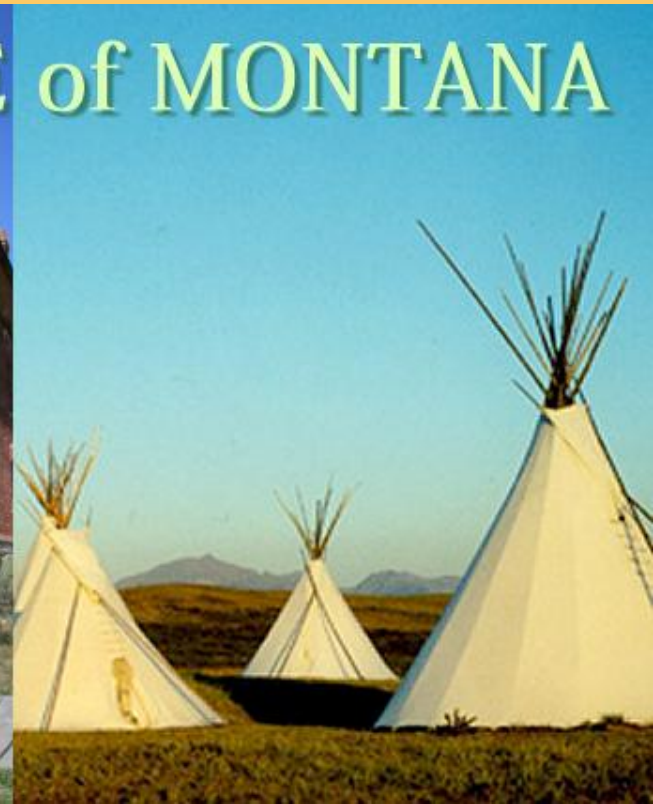
Key Changes - HUD

- In the Yellow Book reports, report subheadings of "Internal Control Over Financial Reporting" and "Compliance and Other Matters;"
 - In the Yellow Book reports, a new "purpose alert" as required by AU-C 905, *Alert that Restricts the Use of the Auditor's Written Communication (AICPA, Professional Standards), for certain engagements performed under Government Auditing Standards;*
 - In the HUD compliance reports, use of major headings to clarify fact that the HUD reporting actually includes several distinct reports—that is, a Report on Compliance for Each Major HUD Program (opinion-level assurance) and a Report on Internal Control over Compliance (byproduct reporting on internal control over compliance);.
- Other geographical changes in reports

Proposed Changes to Federal Grant Audits / Operations and New (Proposed) Data Collection Form

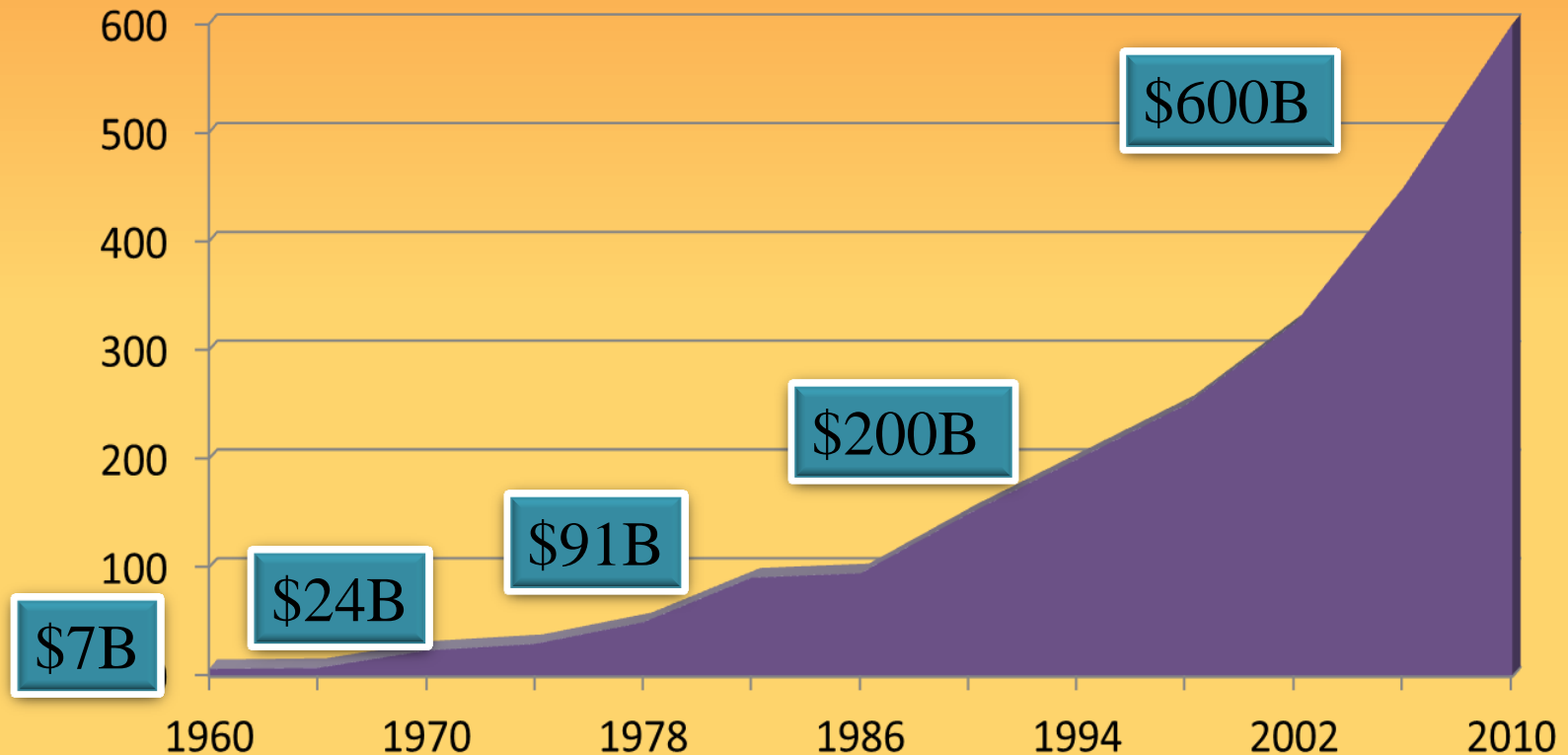


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Why Change? - Increase in Federal Grants Activity

In Billions of \$



The Catalog of Federal Domestic Assistance lists more than 2,000 Federal grant programs

Federal Grants Management Priorities



Grants Circular Reform

Challenge

- Eight overlapping complex sets of guidance
- Federally funded scientists report spending on average 40% of their time on administrative tasks
- Over 4,000 audited programs failed to receive clean opinions in 2011 (3% of total audited programs)
- Major programs report repeat audit findings causing material noncompliance but no easy way to track repeat findings.
- No existing guidance holds agencies and recipients accountable effectively correcting financial integrity weaknesses.

Proposed Reform

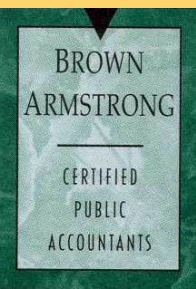
- February 1, 2013- Notice of Proposed Guidance in Federal Register (www.regulations.gov, docket OMB-2013-0001)
- By December 2013 Finalize Guidance

Grants Circular Reform: Proposed Elements

- Administrative Requirements (A-110, A-102, A-89)
 - Require Pre-Award Consideration of Merit/Risk rather than automatic grant awards year after year
 - Streamline and Clarify Guidance on Subrecipient Monitoring
- Cost Principles (A-87, A-21, A-122)
 - Provide Consistency on Negotiated Indirect Cost Rates
 - Simplify Reporting Requirements for Time and Effort
 - Allow direct charging of directly allocable administrative costs

Grants Circular Reform: Proposed Elements

- Single Audit and Audit Follow-up (A-133 & A-50)
 - Target Audit Resources Based on Risk:
 - Raise Threshold From \$500k to \$750k, but still report individual grants on SEFA <\$750k.
 - Revise Definition of “Major Programs” to Focus Audits on Material Issues
 - Reduce from 14 to 7 the types of compliance requirements audited (aka the “cross-cutters”) (6 common, 1 agency specific)
 - Strengthen Audit Follow-up
 - Senior Accountable Official, implement metrics on repeat findings, encourage cooperative audit resolution
 - Make audit reports and management decisions public, allow for reliance on cognizant entity decisions where applicable



Grants Data Standardization

Challenge

- Over 700 distinct grant related forms approved in OMB database – many of them inconsistent between agencies
- Inefficient use of recipient and Federal resources to comply with guidance
- Non-standard data definitions compromise quality of publicly reported financial data

Proposed Deliverables

- By December 2013 issue revised pre and post award standard data elements
- By December 2015 allow any non-standard form approvals to expire

Spending Transparency

Challenge

- Lack of control totals to verify accuracy of spending data and financial data and accountability to stakeholders
- Disparate communities are working to standardize data elements that may overlap but not align
- Lack of high quality information on which to base program management decisions
- Inability to adequately satisfy requests for information

Proposed Deliverable

- By April 2013 publish guidance on leveraging financial data oversight and internal controls for spending data (implemented by January 2014)
- By October 2014 publish payment information repository (Treasury)
- By October 2015 improve quality of publicly reported financial data

Workforce Development

Challenge

- Lack of consistent standards for qualifying people to perform the grants management function
- No government-wide core training required of people performing the grants management function

Proposed Reform

- By September 2013
 - Establish core competencies for grants managers
 - Establish governmentwide resource repository for federal grants professionals – agencies begin leveraging existing resources to train workforce.

Audit Resolution

Challenge

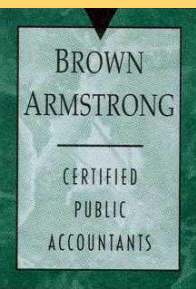
- Over 4,000 audited programs failed to receive clean opinions in 2011 (3% of total audited programs)
- Major programs report repeat audit findings causing material noncompliance, but no easy way to track repeat
- No existing guidance holds agencies and recipients accountable for effectively correcting financial integrity weaknesses
- Lack of prompt follow-up actions leads to unresolved audit findings, which increases risks to program integrity

Proposed Reform

- By October 2013, identify high risk programs, baseline “unclean” audit opinions and material audit findings, and develop a corrective action plan to resolve high risk findings.
- By August 2015, based on FY14 audits, measure the reduction in “unclean” audit opinions on identified programs.
- By December 2015, Council on Financial Assistance Reform will review the results and recommend best practices for audit resolution government-wide.

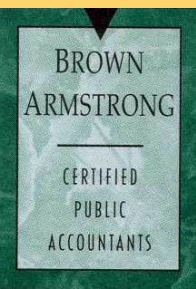
Other Provisions

- Type A and B program coverage may change
 - High risk Type B program testing would be reduced from 50% of Type A low risk programs to 25% of Type A low risk programs.
 - Small Type B programs would be designated as having 25% or less than the final program determination threshold.
 - Programs that are less than 25% of the threshold or \$125,000 would likely not be audited regularly unless risk is present.



Other Provisions

- Questioned cost threshold may raise from \$10,000 to \$25,000 to be reported
- Indirect costs may have major changes
 - If never received indirect cost recoveries - opportunity to recover 10% of modified total direct costs to pay for allowable admin costs for up to four initial years (only).
 - MTDC definition may include all salaries and wages, fringe benefits, materials and supplies, services, travel, and subgrants and subcontracts up to the first \$25,000 of each subgrant or subcontract (regardless of the period covered by the subgrant or subcontract)
 - Equipment, capital expenditures, charges for patient care, rental costs, tuition, participant support costs, and the portion of subcontracts and subawards > \$25,000 excluded from MTDC
- Other rates negotiated will have far more documentation – goal is to have all subject to flat rate after 4 years

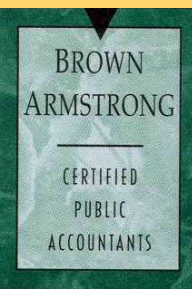


Other Provisions

- Standardized grant applications (aka – the Common App) coming to grants
 - Grant availability must be made publicly available for at least 30 days
- No automatic renewal – renewals based on
 - Financial stability
 - Quality of information and reporting
 - Ability to meet standards and guidelines (e.g. clean opinions)
 - History of management of the grant including timely reporting
- Effective date – one year after all guidance becomes final (could be for 2014 or 2015 audits.)

New for 2013 or 2014 SF-SAC Items

- Page 1 - Auditors Required to Report EIN
- Page 3 - Designation for Federal Loans and Loan Guarantees
- Page 4 – Standardized Finding Reference Number Format – Year hyphen and three digit finding number
- Page 4 – Expanded Information to Allow for Three- way Link
- PDF – Unlocked, Unencrypted, Text Searchable (new function to upload and text 85% encryption requirement began July 2012)



Proposed Solution – should be final soon

- Auditor complete Page 3 by CFDA line
- FAC produce template to generate and pre-populated new Page 4 for CFDA lines based on indicated number of audit findings
- Auditor complete Page 4 template to provide information by audit finding number.
 - Finding reference number (consistent format)
 - Type of compliance requirement
 - Type of finding (Modified Opinion, Other N/C, MW, SD, Other)
 - Questioned costs – Y or N



2013 or 2014 Form SF-SAC Page 3

Proposed

Form SF-SAC Single Audit Data Collection Form										REPORT ID:419455		VERSION:2	
Part III: FEDERAL PROGRAMS Continued													
9. FEDERAL AWARDS EXPENDED DURING FISCAL YEAR													
Page 3 Row Number	CFDA Number		R&D(c)	Loan/Loan Guarantee (d)	ARRA(e)	Name of Federal program (f)	Amount expended (g)	Direct award (h)	Major program		Number of Findings (k)		
	Federal Agency Prefix (a)	Extension (b)							Major program (i)	If yes, type of audit report (j)			
1	93	001	N	N	N	Example Program 1	\$613,265	Y	Y	Q	1		
2	93	002	N	N	N	Example Program 2	\$729,397	Y	Y	A	1		
3	93	003	N	N	N	Example Program 3	\$450,516	Y	Y	Q	1		
4	93	004	N	N	N	Example Program 4	\$422,922	Y	Y	U	2		
5	93	005	N	N	N	Example Program 5	\$305,678	Y	Y	U	2		
6	93	006	N	N	N	Example Program 6	\$1,206,013	N	Y	U	1		
7	93	007	N	N	N	Example Program 7	\$3,198,818	Y	Y	U	1		
8	93	008	N	N	N	Example Program 8	\$185,264	Y	N	U	0		
9	93	009	N	N	N	Example Program 9	\$988,176	Y	Y	U	1		
10	93	010	N	N	N	Example Program 10	\$1,200,369	Y	Y	U	1		
11	93	011	N	N	N	Example Program 11 CFDA line a	\$435,982	Y	Y	U	1		
12	93	011	N	N	N	Example Program 11 CFDA line b	\$173,906	Y	Y	U	1		
13	93	011	N	N	N	Example Program 11 CFDA line c	\$729,881	Y	Y	U	1		
14	93	012	N	N	N	Example Program 12 Part of Cluster X	\$399,841	Y	Y	Q	1		
15	93	013	N	N	N	Example Program 13 Part of Cluster X	\$900,157	Y	Y	Q	1		
16	93	014	N	N	N	Example Program 14 Part of Cluster X	\$100,397	Y	Y	Q	0		
TOTAL FEDERAL AWARDS EXPENDED ----->							\$12,040,582						

NEW FIELD

NEW FIELD

Example of programs with multiple findings. Page 4 will have corresponding number of lines (in this case two)

Example of program with no findings - Not appear on Page 4

Example of finding and multiple CFDA lines.

Example of cluster with qualified opinion and finding not affecting all CFDA's. Qualified opinion runs to cluster. FAC Edit will change to allow modified opinion and no finding.

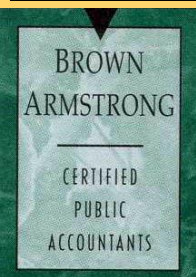
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2013 or 2014 Proposed Page 4 Completed Example

Page 3 Row Number (a)	CFDA Prefix (b)	CFDA Extension (c)	Name of Federal program (f)	Finding Reference Number (d)	Type(s) of Compliance Requirement(s) (e)	Types of Finding					Questioned Costs? Y/N (k)	
						Modified Opinion (f)	Other NonCompliance (g)	Material Weakness (h)	Significant Deficiency (i)	Other (j)		
1	93	001	Example Program 1	2013-001	E	X					N	Example of all 9 possible combinations of types of findings.
2	93	002	Example Program 2	2013-002	AB	X		X			Y	
3	93	003	Example Program 3	2013-003	I	X			X		Y	
4	93	004	Example Program 4	2013-004	J		X				N	
4	93	004	Example Program 4	2013-005	C		X	X			N	
5	93	005	Example Program 5	2013-006	I		X		X		N	
5	93	005	Example Program 5	2013-007	E			X			N	
6	93	006	Example Program 6	2013-008	F				X		N	
7	93	007	Example Program 7	2013-009	N					X	N	
9	93	009	Example Program 9	2013-002	AB	X		X			Y	Example finding affecting multiple programs-same type of finding (93.002 & 93.009)
10	93	010	Example Program 10	2013-003	I				X		N	Example finding affecting multiple programs-different type of finding (93.003 & 93.010)
11	93	011	Example Program 11 CFDA line a	2013-010	G		X				N	Example of finding and multiple CFDA lines
12	93	011	Example Program 11 CFDA line b	2013-010	G		X				N	
13	93	011	Example Program 11 CFDA line c	2013-010	G		X				N	
14	93	012	Example Program 12 Part of Cluster X	2013-011	E	X		X			N	Example of cluster with finding affecting only some of programs in cluster.
15	93	013	Example Program 13 Part of Cluster X	2013-011	E	X		X			N	



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2013 or 2014 Page 4 Completed Example

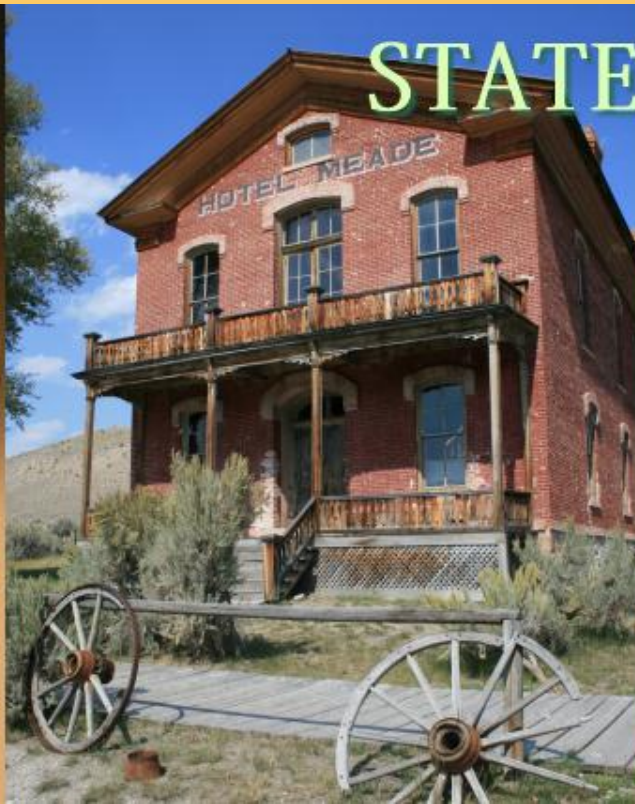
Page 3 Row Number (a)	CFDA Prefix (b)	CFDA Extension (c)	Name of Federal program (f)	Finding Reference Number (d)	Type(s) of Compliance Requirement(s) (e)	Types of Finding					Questioned Costs? Y/N (k)	
						Modified Opinion (f)	Other NonCompliance (g)	Material Weakness (h)	Significant Deficiency (i)	Other (j)		
1	93	001	Example Program 1	2013-001	E	X					N	Example of all 9 possible combinations of types of findings.
2	93	002	Example Program 2	2013-002	AB	X		X			Y	
3	93	003	Example Program 3	2013-003	I	X			X		Y	
4	93	004	Example Program 4	2013-004	J		X				N	
4	93	004	Example Program 4	2013-005	C		X	X			N	
5	93	005	Example Program 5	2013-006	I		X		X		N	
5	93	005	Example Program 5	2013-007	E			X			N	
6	93	006	Example Program 6	2013-008	F				X		N	
7	93	007	Example Program 7	2013-009	N					X	N	
9	93	009	Example Program 9	2013-002	AB	X		X			Y	Example finding affecting multiple programs-same type of finding (93.002 & 93.009)
10	93	010	Example Program 10	2013-003	I				X		N	Example finding affecting multiple programs-different type of finding (93.003 & 93.010)
11	93	011	Example Program 11 CFDA line a	2013-010	G		X				N	Example of finding and multiple CFDA lines
12	93	011	Example Program 11 CFDA line b	2013-010	G		X				N	
13	93	011	Example Program 11 CFDA line c	2013-010	G		X				N	
14	93	012	Example Program 12 Part of Cluster X	2013-011	E	X		X			N	Example of cluster with finding affecting only some of programs in cluster.
15	93	013	Example Program 13 Part of Cluster X	2013-011	E	X		X			N	

2011 / 12 Yellow Book

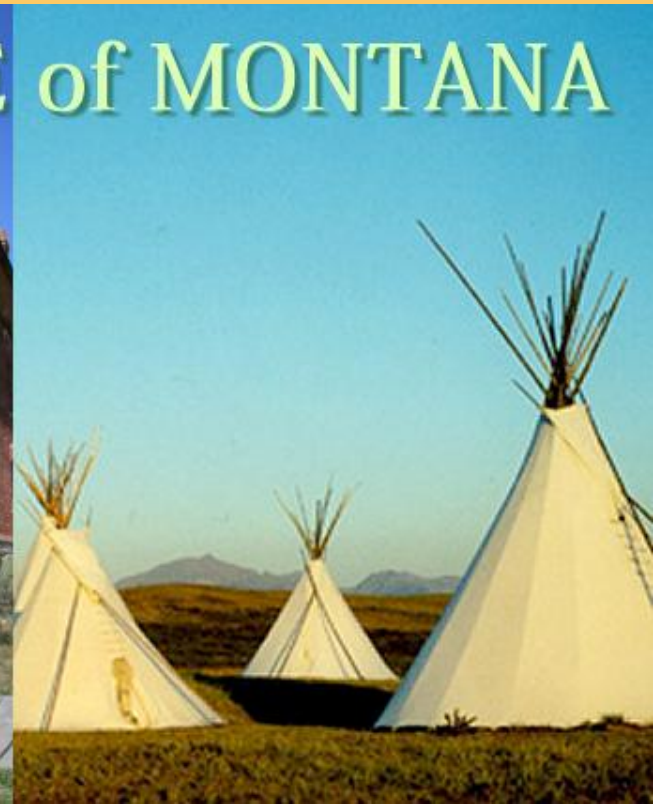
Recent discussions - Independence



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Chapter 3:

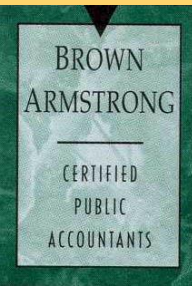
General Standards

- Independence
 - Conceptual framework
 - Provision of nonaudit services to auditees
- Professional judgment
- Competence
 - Technical knowledge
 - Continuing Professional Education
- Quality Assurance
 - System of quality assurance
 - Peer review



Independence Timeframes

- Impairment exists during
 - The period of the audit – usually the fiscal year
 - The professional engagement
 - usually starts with earlier of start of planning or engagement agreement.
 - usually ends on the last report date.
- Depending on the circumstances, independence may be impacted beyond this timeframe.
- Recurring engagement may mean that some activities or circumstances will always impair.



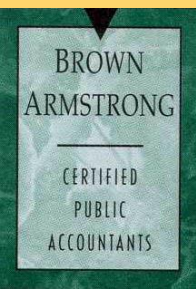
Applying the Framework

Threats *could* impair independence

- Do **not** necessarily result in an independence impairment

Safeguards *could* mitigate threats

- Eliminate or reduce to an acceptable level



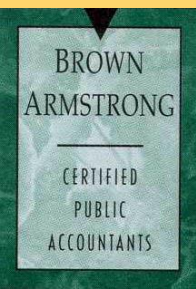
Applying the Framework

Conceptual Framework:

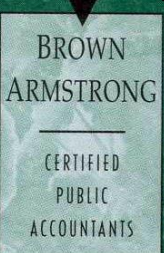
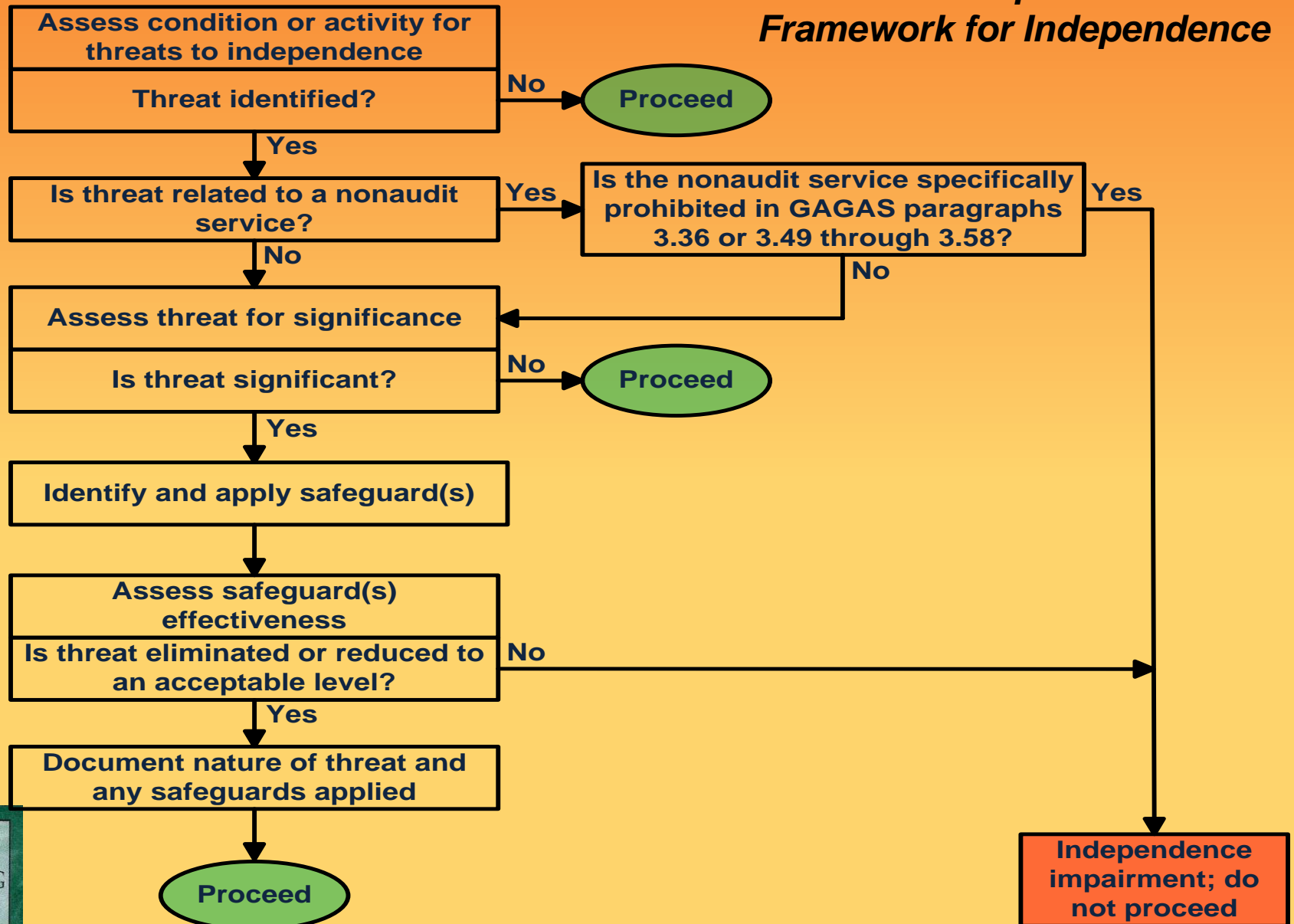
1. Identify threats to independence
2. Evaluate the significance of the threats identified, both individually and in the aggregate
3. Apply safeguards as necessary to eliminate the threats or reduce them to an acceptable level
4. Evaluate whether the safeguard is effective

Documentation Requirement:

Para 3.24: When threats are not at an acceptable level and require application of safeguards, auditors should document the safeguards applied.



GAGAS Conceptual Framework for Independence



Applying the Framework: Categories of Threats

1. Management participation threat
2. Self-review threat
3. Bias threat
4. Familiarity threat
5. Undue influence threat
6. Self interest threat
7. Structural threat

Independence:

Examples of Safeguards

- **Mitigate to an acceptable level by:**
 - Reassigning individual staff members who may have a threat to independence.
 - Having separate staff perform the nonaudit and audit services.
 - Having professional staff from outside of the team review the work.
 - Using or consulting with an independent third party.
 - Involving another audit organization.
- **Decline to do the requested scope of the nonaudit service.**

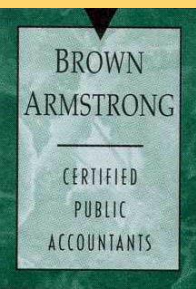


Routine Audit Services and Nonaudit Services

Routine audit services pertain directly to the audit and include:

- Providing advice related to an accounting matter
- Researching and responding to an audited entity's technical questions
- Providing advice on routine business matters
- Educating the audited entity on technical matters

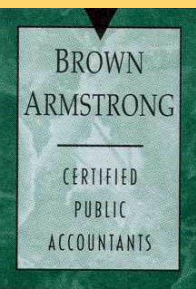
Other services not directly related to the audit are considered nonaudit services



Routine Audit Services and Nonaudit Services

Services that are specifically identified as nonaudit services include:

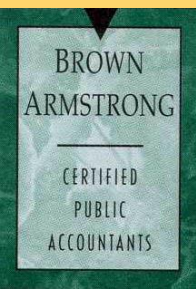
- Financial statement preparation
- Bookkeeping services
- Cash to accrual conversions (a form of bookkeeping)
- Other services not directly related to the audit
- Tax Preparation (not for profits)



Nonaudit Services

1. Determine if there is a specific prohibition.
Unless specifically prohibited, nonaudit services MAY be permitted but should be documented.
2. If not prohibited, assess the nonaudit service's impact on independence using the conceptual framework.
3. If the auditor assesses any identified threat to independence as higher than insignificant, assess the sufficiency of audited entity management's skill, knowledge, and experience to oversee the nonaudit service.

And...

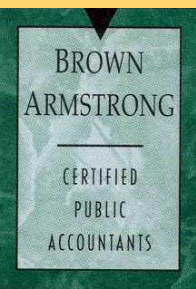


Nonaudit Services (Continued)

4. If the auditor concludes that performance of the nonaudit service will not impair independence, document assessments in relation to both:
- safeguards applied in accordance with the conceptual framework and
 - the auditor's assessment of sufficiency of audited entity managements' skill, knowledge or experience to oversee the nonaudit service (paragraph 3.34).

Assessing Management's Skill, Knowledge, or Experience

- Factors to document include management's:
 - Understanding of the nature of the nonaudit service
 - Knowledge of the audited entity's mission and operations
 - General business knowledge
 - Education
 - Position at the audited entity
- Some factors may be given more weight than others
- GAGAS does not require that management have the ability to perform or reperform the service



Sufficiency of Skills, Knowledge and Experience

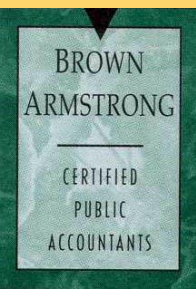
- Sufficient skills, knowledge and experience may be judged based in part on:
 - Ability of the responsible audited entity personnel to understand the nature and results of the nonaudit service
 - Ability of the responsible person to identify material errors or misstatements in a nonaudit service work product
 - Ability and willingness and of the responsible person to take meaningful action in the event of identification of a problem with the nonaudit service
- Client prepared material in poor condition may indicate the client is not capable of taking responsibility for the service. Significant audit findings and adjustments may also be indicative of this issue.



Financial Statement Preparation

Auditors *may* prepare financial statements

- Considered by GAGAS a non-audit service
- Must apply the conceptual framework
- Two additional documentation requirements:
 - Document application of safeguards
 - Document assessment of management's skill, knowledge or expertise
 - See previous on lack of skill, knowledge or expertise

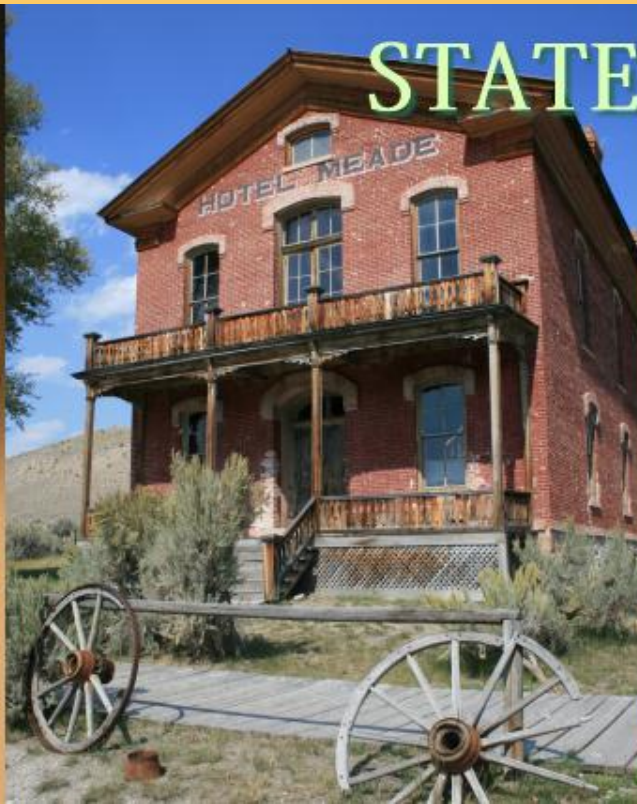


A Few Questions on Fraud

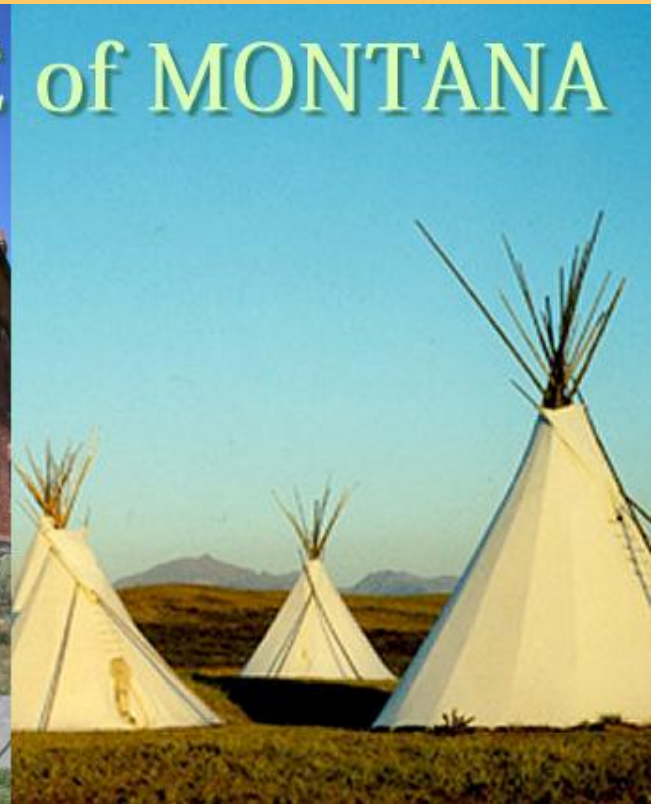
Take a few minutes and discuss among yourselves
WAGERING IS ALLOWED!



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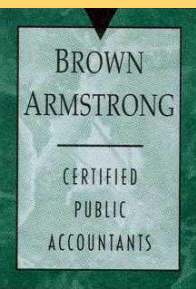


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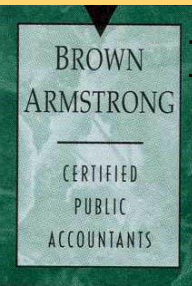
Given the increased importance of, and attention to, protecting corporate intellectual property and sensitive customer and employee information, the area of information technology (IT) governance is a growing concern for many boards. Which of the following is true regarding how boards are addressing this issue?

- a. The majority of boards are creating separate IT risk committees to address IT governance issues.
- b. Boards are adding younger directors to increase the boards' overall familiarity with IT issues and risks.
- c. Boards increasingly are engaging outside IT experts to advise them on IT risks and issues.
- d. The majority of boards are spending 20% or more of their meetings discussing IT-related risks and issues.



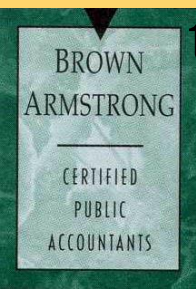
One of the main benefits of using data analysis techniques to detect fraud is that:

- a. They can provide insight into the details of how a fraud occurred.
- b. They can be used to establish predication for a full fraud examination.
- c. They are easily performed using off-the-shelf tools that enable anyone to undertake an in-depth analysis without specific technological knowledge.
- d. They can take the place of the fraud risk assessment in identifying key areas of fraud risk within the organization.

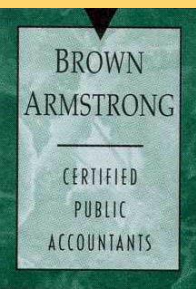


Which is the most effective order of steps in the data analysis process?

- a. Build a profile of potential frauds; obtain the data; verify the data; cleanse the data; analyze the data.
- b. Obtain the data; cleanse the data; analyze the data; verify the data; build a profile of potential frauds.
- c. Obtain the data; analyze the data; cleanse the data; verify the data; build a profile of potential frauds.
- d. Build a profile of potential frauds; verify the data; obtain the data; cleanse the data; analyze the data.

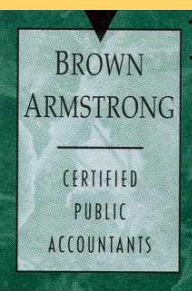


The audit department of a government received a tip that a few employees have been colluding to siphon off taxpayer data and sell it to an organized crime ring for use in identity theft schemes. To help identify whether such a scheme is occurring and who might be involved, the internal audit team decides to employ textual analytics techniques to inter-employee communications. Which of the following combinations of keywords or phrases likely would be the most helpful in identifying communications between the data thieves regarding their scheme? (See next slide)

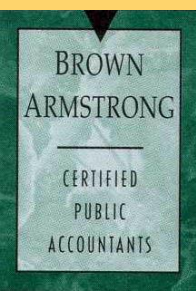


Continued from Previous

- a. “Confidential” and “taxpayer information.”
- b. “Confidential”; “unauthorized copying”; and “nobody will notice.”
- c. “Nobody will notice” and “not hurting anyone.”
- d. “Unauthorized copying” and “taxpayer information.”

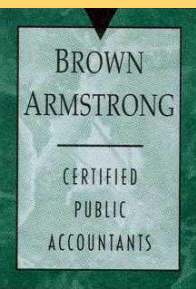


Diana, a CPA, is the controller for a City. She receives a call from Joshua, the accounts receivable manager of Circle Corp., one of the City's vendors, regarding numerous double payments received from the City during the past six months. Joshua says he does not understand why the invoices are being paid twice and that he would like to get the situation straightened out to avoid having to continue issuing refund checks to the City. He also says that he usually deals with Amanda, The City's accounts payable manager, but that she has not been able to curb the situation, so he thought he would try taking it to her boss. After hanging up the phone, Diana pulls up Circle Corp.'s accounts payable history to try to figure out what's going on, but she sees no sign of duplicate payments or refunds. Growing concerned, she decides to run some data analytics tests on payments to vendors to see if she can find any other anomalies. Which of the following fields would be LEAST helpful in searching for clues regarding duplicate payments to vendors in The City's accounting system?



Continued from Previous

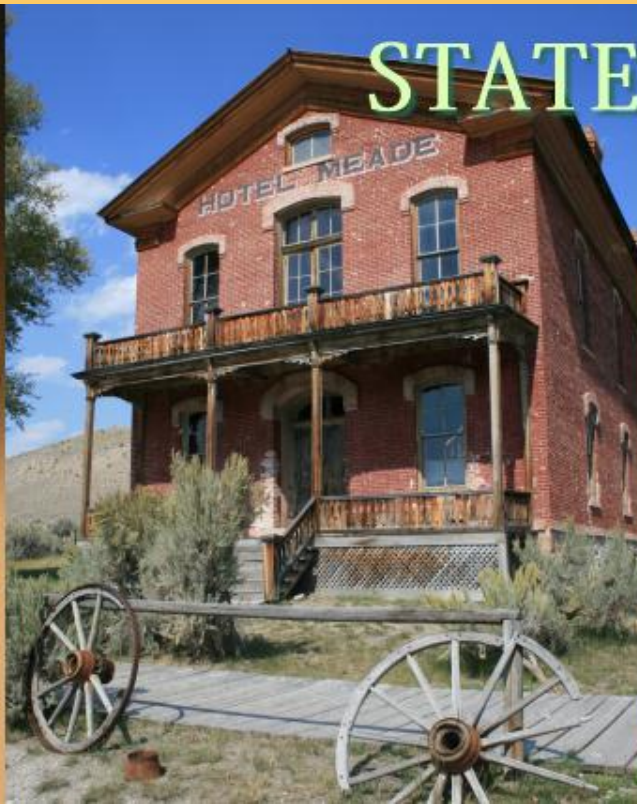
- a. Vendor address.
- b. Vendor number.
- c. Invoice number.
- d. Payment amount



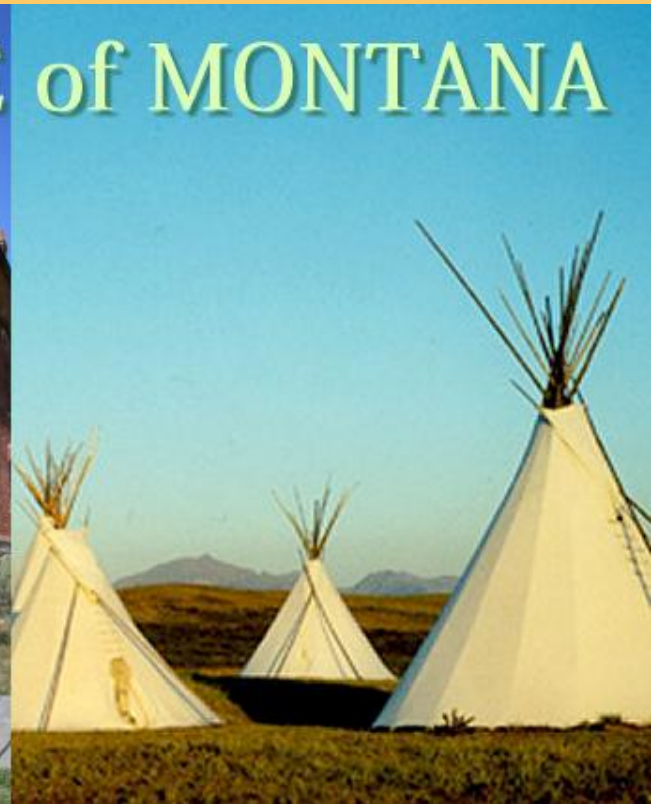
Ethics... Ethics...
Ethics...



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—
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PUBLIC
ACCOUNTANTS



STATE of MONTANA



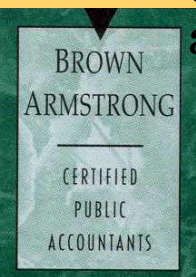
Who are We and Why Did We Get Here?



KPMG partner Scott London, left, is shown in an FBI photograph allegedly accepting a \$5,000 cash bribe from Bryan Shaw earlier this year. Federal prosecutors have charged London with providing Shaw inside information on two California companies, Herbalife Ltd. and Skechers USA Inc. (U.S attorney's office)

The Charges Against Mr. London

- The KPMG insider trading scam was far more profitable than earlier known and went longer than thought.
- Scott London, the disgraced ex-auditor from KPMG's office in Los Angeles, has been charged in a federal complaint with one count of conspiracy to commit securities fraud through insider trading.
- The 24-page affidavit alleges that London provided confidential information about KPMG clients to Bryan Shaw, a close friend, over a period of several years and that Shaw used this information to make highly profitable securities trades that generated more than \$1 million in illegal proceeds.
- In an interview with The LA Times, London had claimed the insider tips only led to a profit of about \$100,000 for Shaw.
- The criminal complaint filed in federal court also portrays London as far more culpable and intimately involved in all details of the trading scandal than he had previously acknowledged with The LA Times and other media outlets.



The Charges Against Mr. London

- In a separate action, the U.S. Securities and Exchange Commission (SEC) announced the filing of civil charges against London and Shaw.
- From late 2010 and continuing until March 2013, London secretly passed "highly sensitive and confidential information" to Shaw regarding upcoming earnings announcements by certain KPMG clients, including [Herbalife](#), Skechers, and [Deckers Outdoor Corp.](#), before that financial information was disclosed to the public.
- In exchange, Shaw gave London tens of thousands of dollars in cash, typically instructing London to meet him on a side street near Shaw's business in order to give him bags containing \$100 bills wrapped in \$10,000 bundles.



Ethical Lapses are Everywhere

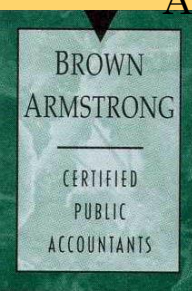
Former Treasurer Accused of Embezzling from Institute of Internal Auditors' D.C. Chapter
WASHINGTON, D.C. (APRIL 8, 2013)

BY MICHAEL COHN

The former president and treasurer of the Washington, D.C., chapter of the Institute of Internal Auditors has been accused of embezzling over \$30,000 from the organization. Robin Howard, who had also served as former director of audit services for Prince William County, Va., may have stolen up to \$50,000 from the organization. The missing funds were discovered after another treasurer succeeded Howard.

“Our Washington, D.C., chapter had noticed when they had an officer transition this past year that when they were looking at the bank statements and the chapter financial statements that were issued, that there was a large discrepancy between what showed in the bank account and what was actually reported on the financial statements,” said Kevin Mayeux, general counsel and chief operating officer at the IIA. “Then at that point, the chapter leadership went out and engaged a third-party forensic accountant to take a look at the matter, to thoroughly investigate in an independent way what the differences are and why, and then after that believed that there were some significant funds unaccounted for and they turned the matter over to the authorities for their investigation and potential prosecution.”

A bench warrant was issued for Howard last Tuesday in Prince William County, but as of last Friday he had not been arrested.



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Former Treasurer Accused of Embezzling from Institute of Internal Auditors' D.C. Chapter

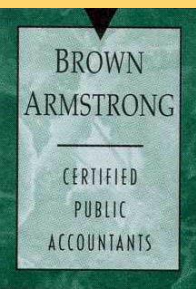
Prosecutors have charged Howard with stealing \$50,000 from the Washington, D.C., chapter. "There are \$30,000 directly confirmed as unexplained distributions or disbursements, and upwards to approximately an additional \$20,000 that are still to be confirmed," said Mayeux. The alleged misappropriation took place between October 2009 and August 2011.

Mayeux noted that the D.C. chapter has undertaken a thorough review of its internal control processes in the wake of the discovery of the missing funds. The IIA national headquarters has also formed a task force to look at revising and enhancing its recommended internal controls for chapter around the world. The IIA often provides information to internal auditors on how to improve their internal controls, and the case may become a kind of lesson learned for the organization itself. "That's certainly how we'll use it with our membership so we that can continue to improve," said Mayeux.

The IIA also released a statement explaining the situation. "The Institute of Internal Auditors Global Headquarters is extremely disappointed by the alleged misappropriation of assets that occurred in our Washington, D.C., chapter," the organization said in a statement forwarded by a spokesman. "This is a matter we take very seriously and we are working with our local leadership to take all steps necessary to recover the funds and prosecute the individual allegedly responsible for these actions.

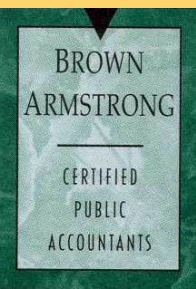
"As soon as we were made aware of the situation by IIA-Washington, D.C., we took immediate steps to launch an investigation. We continue to work closely with IIA-Washington, D.C., to support their steps in seeing justice served. They are able to continue providing their regular programming and member benefits. We all strongly believe in and understand the tenets of strong governance and financial oversight, and we have taken steps to better ensure this does not happen again.

"All IIA chapters have a uniform set of internal controls recommended by IIA Headquarters. We are working closely with all of our volunteer chapter leaders to ensure full understanding of these recommended controls for chapter financial management. We assumed each person entrusted with financial responsibility in our chapter shared the same values we believe to be common within the internal audit profession including honesty, integrity and professionalism."



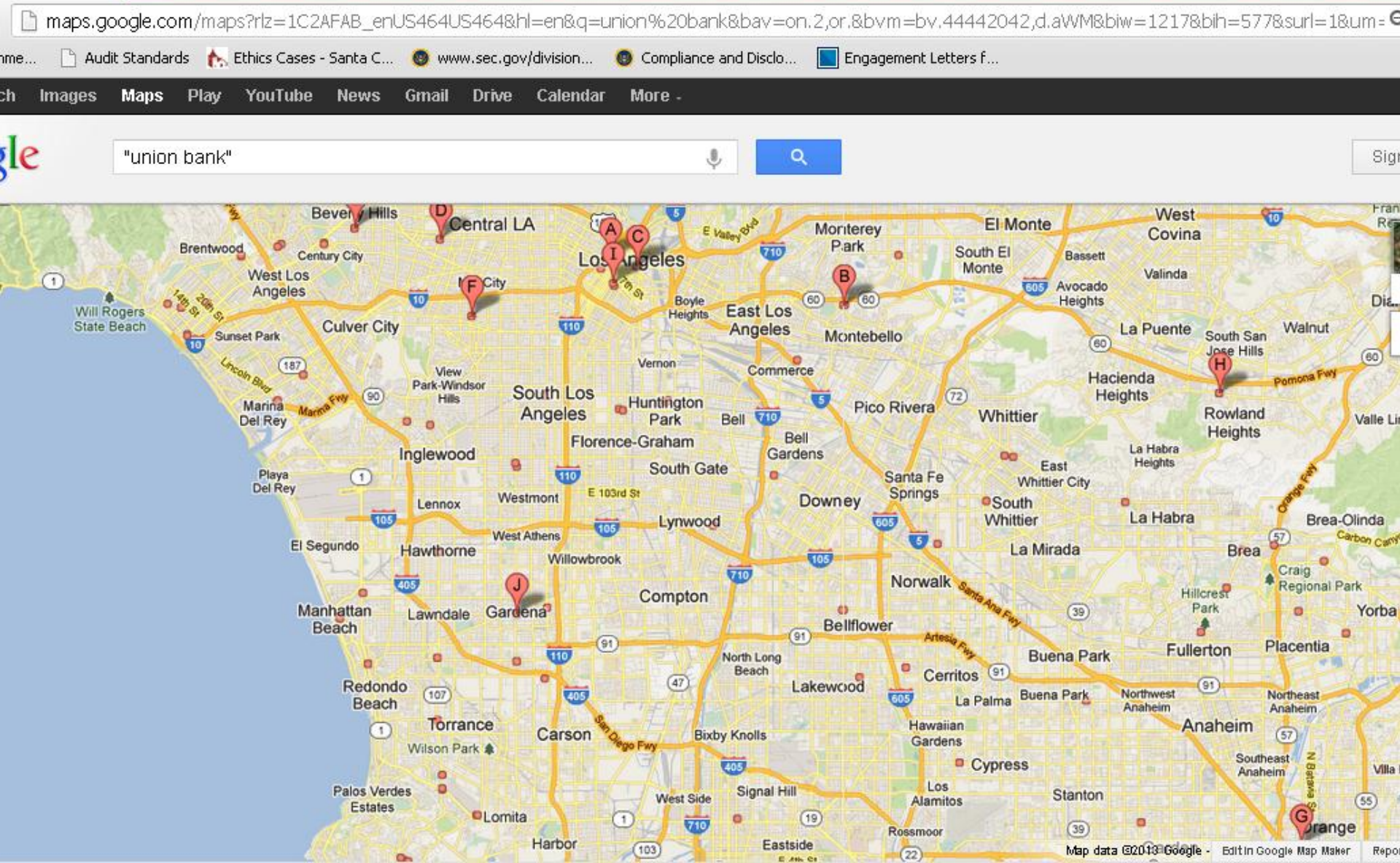
The Curious Campaign by Union Bank

<http://www.youtube.com/user/unionbank>

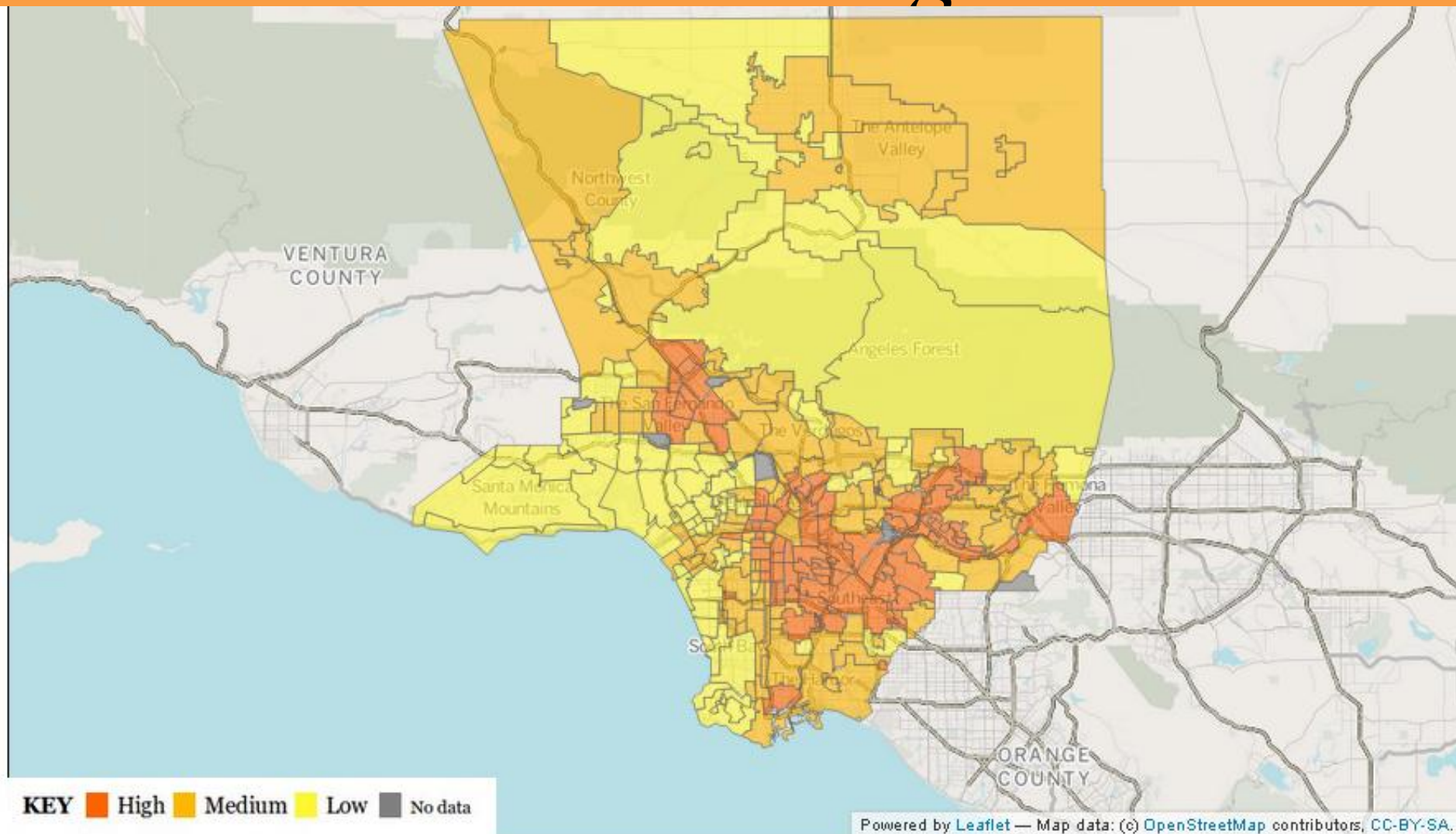


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But – Is It Ethical? What Do You See By the Following Maps?



Latino Los Angeles



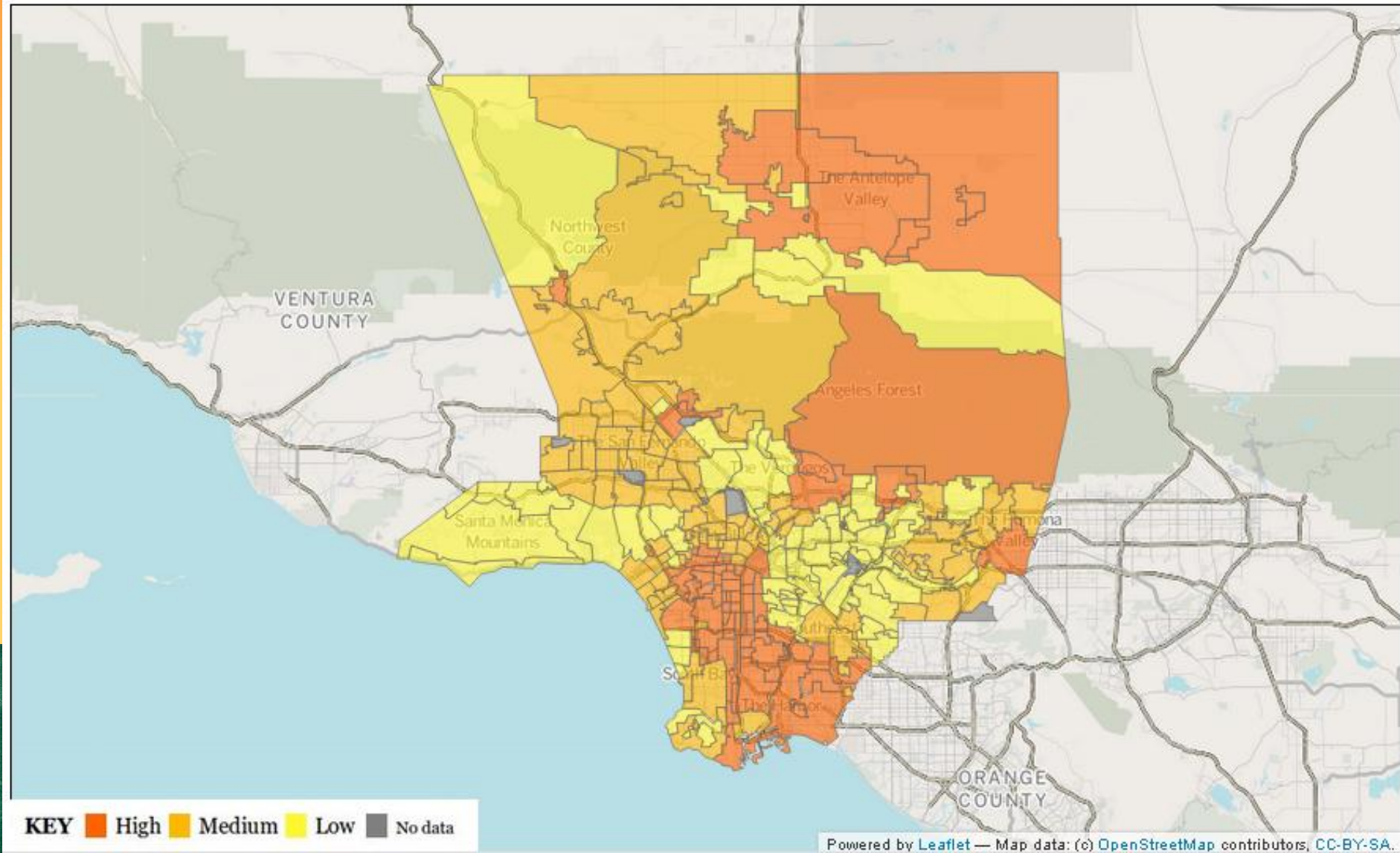
The percentage of the population of whose ethnicity is **Latino**.

There are rankings available for [asian](#), [black](#), [Latino](#) and [white](#).

Mapping L.A. is the Los Angeles Times'

African American Los Angeles

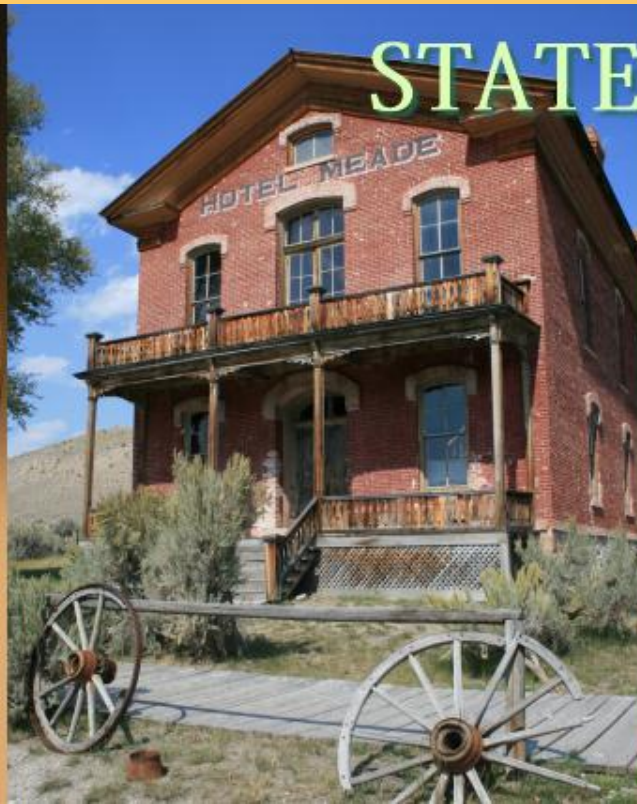
Select one of L.A.'s 272 neighborhoods to see where it ranks



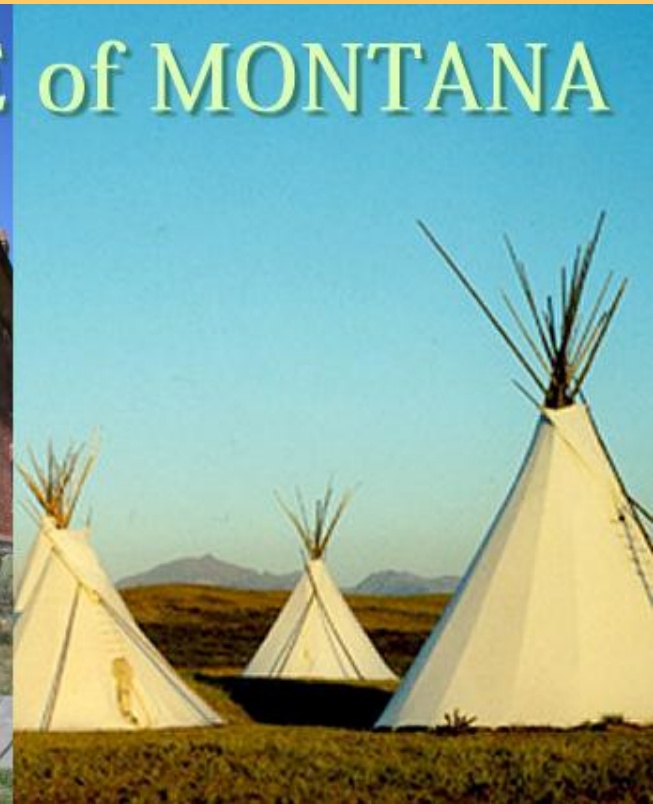
Professional Ethics – the New (and Improved?) Codified AICPA Professional Ethics – EXPOSURE DRAFT



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Key Items in the New Code Exposure Draft Released 4/15/13

- Comments due 8/15/13
- Revised Code may migrate to a “threats and safeguard” approach similar to GAGAS.
- New Structure of Code
 - Preface which is applicable to all members and covers topics such as the structure of the AICPA Code
 - Principles
 - Defined terms
 - Nonauthritative Guidance
 - New / Revised / Pending Interpretations



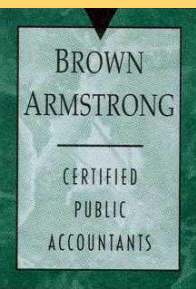
Key Items in the New Code Exposure Draft Released 4/15/13

- New Structure of Code
 - Remaining three parts are divided according to member's practice
 - Part 1: Members in public practice (firms)
 - Part 2: Members in business (employers)
 - Part 3: All other members such as those who are retired or unemployed
- New Numeric Citations
 - ET Sections would be renumbered
 - Preface 0.XXX.XXX (First XXX = topic)
 - Part 1: 1.XXX.XXX (Second XXX = subtopic)
 - Part 2: 2.XXX.XXX (Could be subsections)
 - Part 3: 3.XXX.XXX



Key Items in the New Code Exposure Draft Released 4/15/13

- Rules of Conduct unchanged
- Specific Rule Numbers No Longer Used
 - Rule 101, *Independence* is now referred to as the —*Independence Rule*
 - Contingent Fees Rules and —Commission and Referral Fees Rules and related interpretations appear under ET section 1.500, —Fees and Other Types of Remuneration (AICPA, *Professional Standards*)



Key Items in the New Code Exposure Draft Released 4/15/13

- *Use of Should Consider, Consider Evaluate, or Determine*
 - *Consider* is used when the member is required to think about several matters.
 - *Evaluate* is used when the member has to assess and weigh the significance of a matter
 - *Determine* is used when the member has to conclude and make a decision.

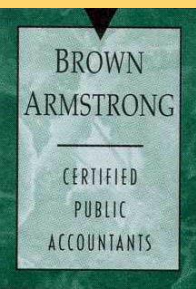


Key Items in the New Code Exposure Draft Released 4/15/13

- **Substantive Changes**

- Two New Conceptual Framework interpretations to the AICPA Code

- **Members in Business** - (ET section 2.000.010,
—Conceptual Framework for Members in Business||
[AICPA, *Professional Standards*])
 - **Members in Public Practice** – (ET section 1.000.010,
—Conceptual Framework for Members in Public
Practice|| [AICPA, *Professional Standards*]).
 - **New Interpretations Under Each Rule** - (for example, ET
sections 1.100.005 and 2.100.005 [AICPA, *Professional
Standards*])



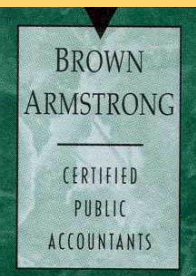
Key Items in the New Code Exposure Draft Released 4/15/13

- **Self Review Threat Definition Redone**
 - Former Definition:
 - **.13 *Self-review threat***—Members reviewing as part of an attest engagement evidence that results from their own, or their firm's, nonattest work such as, preparing source documents used to generate the client's financial statements
 - **Proposed Definition** (paragraph .16 of ET section 1.210.010):
 - **.16 Self-review threat.** The threat that a member will not appropriately evaluate the results of a previous judgment made, or service performed or supervised by the member or an individual in the member's firm, and that the member will rely on that service in forming a judgment as part of an attest engagement. Certain self-review threats, such as preparing source documents used to generate the attest client's financial statements [ET section 1.295.120 (AICPA, Professional Standards)], pose such a significant self-review threat that no safeguards can eliminate or reduce the threats to an acceptable level.



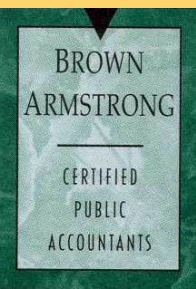
Key Items in the New Code Exposure Draft Released 4/15/13

- Other Substantive Changes Proposed covering
 - Ethical Conflicts
 - Attest Clients and Independence
 - Director's Positions with Banks
 - Tax Power of Attorney and Prospective Clients Confidential Information
 - False, Misleading or Deceptive Acts
 - Billing for Subcontractor's Services
 - Attest Engagements Performed by Former Partners
 - Use of AICPA Award Designations (PFS designations)
 - Loans and Lending Institutions
 - Blind Trusts
- Proposed Effective Date - December 15, 2014
 - Exception for the two broad conceptual frameworks (—Conceptual Framework for Members in Public Practice and —Conceptual Framework for Members in Business). The two broad conceptual frameworks will be given an additional one year delayed effective date.



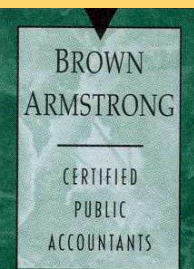
Typical Setup

- 1.700 Confidential Information
 - 1.700.001 Confidential Client Information Rule
 - .01 A member in public practice shall not disclose any confidential client information without the specific consent of the client.
 - 1.700.005 Application of the Conceptual Framework for Members in Public Practice
 - .01 In the absence of an interpretation of the —Confidential Client Information Rule (AICPA, Professional Standards, ET sec. 1.700.001) that addresses a particular relationship or circumstance, a member should apply the —Conceptual Framework for Members in Public Practice.
 - .02 A member will be considered in violation of the —Confidential Client Information Rule if the member cannot demonstrate that safeguards were applied that eliminated or reduced significant threats to an acceptable level.



Mapping Document in Appendix

Extant Code Citations	Title In Code	New Citation In Code	Title In Codification
Introduction	Composition, Applicability, and Compliance	0.100.010	Rules of Conduct
Introduction	Other Guidance	0.100.020	Interpretations and Other Guidance
New		0.200.010	Structure of the AICPA Code
ET section 91	Applicability	0.200.020	Application of the AICPA Code
New		0.200.030	Citations to Prior ET Sections
New		0.200.040	Transition Provisions
ET section 51	Preamble	0.300.010	Preamble
ET section 52	Article I - Responsibilities	0.300.020	Responsibilities
ET section 53	Article II - The Public Interest	0.300.030	The Public Interest
ET section 54	Article III - Integrity	0.300.040	Integrity
ET section 55	Article IV - Objectivity and Independence	0.300.050	Objectivity and Independence
ET section 56	Article V - Due Care	0.300.060	Due Care
ET section 57	Article VI - Scope and Nature of Services	0.300.070	Scope and Nature of Services
ET section 92	Definitions	0.400.00	Definitions
ET Section 101.20	Application of the Independence Rules to Affiliates - Definitions	0.400.01	Affiliate
New		0.400.02	Attest Client
ET section 92.01	Attest engagement	0.400.03	Attest Engagement
ET section 92.02	Attest engagement team	0.400.04	Attest Engagement Team



STATE of MONTANA

Mapping Document in Appendix

ET Section 101.17	Financial Relationships - Definitions	0.400.05	Beneficially Owned
ET section 92.03	Client	0.400.06	Client
ET section 92.04	Close relative	0.400.07	Close Relative
ET section 92.05	Confidential Client Information	0.400.08	Confidential Client Information
Various locations		0.400.09	Control (s) (led)
ET section 92.06	Council	0.400.10	Council
ET section 92.07	Covered Member	0.400.11	Covered Member
ET Section 101.17	Financial Relationships - Definitions	0.400.12	Direct financial interest
ET Section 101.17	Financial Relationships - Definitions	0.400.13	Financial interest
ET Section 101.20	Application of the Independence Rules to Affiliates - Definitions	0.400.14	Financial statement attest client
ET section 92.10	Financial statements	0.400.15	Financial statements
ET section 92.11	Firm	0.400.16	Firm
ET section 92.13	Immediate family	0.400.17	Immediate family
ET Section 100-1	Conceptual Framework for AICPA Independence Standards - Definitions	0.400.18	Independence
ET Section 101.17	Financial Relationships - Definitions	0.400.19	Indirect financial interest
ET section 92.14	Individual in a position to influence the attest engagement	0.400.20	Individual in a position to influence the attest engagement
ET section 92.15	Institute	0.400.21	Institute
ET section 92.16	Interpretation of a rules of conduct	0.400.22	Interpretation
ET section 92.17	Joint closely held investment	0.400.23	Joint Closely Held Investments
ET section 92.18	Key position	0.400.24	Key position
ET section 92.09	Financial institution	0.400.25	Lending institution
ET section 92.19	Loan	0.400.26	Loan
ET section 92.20	Manager	0.400.27	Manager
ET section 92.21	Member	0.400.28	Member
ET section 92.22	Member in business	0.400.29	Member in business
ET section 92.23	Network	0.400.30	Network
ET section 92.24	Network Firm	0.400.31	Network Firm

Mapping Document in Appendix

ET section 92.25	Normal Lending Procedures, Terms, and Requirements	0.400.32	Normal lending procedures, terms, and requirements
ET section 92.26	Office	0.400.33	Office
ET section 92.27	Partner	0.400.34	Partner
ET section 92.28	Partner Equivalents	0.400.35	Partner Equivalents
ET section 92.29	Period of the professional engagement	0.400.36	Period of the professional engagement
ET section 92.30	Practice of public accounting	0.400.37	Public Practice (also referred to as the practice of public accounting)
ET section 92.31	Professional services	0.400.38	Professional Services
ET Section 100-1	Conceptual Framework for AICPA Independence Standards - Definitions	0.400.39	Public interest entities
ET Section 100-1	Conceptual Framework for AICPA Independence Standards - Definitions	0.400.40	Safeguards
ET Section 101.02	Interpretation of Rule 101-Application of the Independence Rules to Covered Members Formerly Employed by a Client or Otherwise Associated with a Client	0.400.41	Share-based compensation arrangements
ET section 92.32	Significant influence	0.400.42	Significant influence
ET Section 101.05	Performance of nonattest services - Management Responsibilities	0.400.43	Source Documents
ET Section 191.224-.225	Use of a Third-Party Service Provider to Assist a Member in Providing Professional Services	0.400.44	Third-party service provider
ET Section 291.023-.024	Applicability of General and Technical Standards When Using a Third-Party Service Provider	0.400.44	Third-party service provider
ET Section 391.001-.002	Use of a Third-Party Service Provider to Provide Professional Services to Clients or Administrative Support Services to the Member	0.400.44	Third-party service provider

Mapping Document in Appendix – another 10 pages of mapping

New		0.500.000	Nonauthoritative Guidance
New		0.600.010	New and Revised Interpretations
New		0.600.020	Pending Interpretations
New		0.700.000	Deleted Interpretations
New		1.000.000	Members in Public Practice - Introduction
New		1.000.010	Conceptual Framework for Members in Public Practice
New		1.000.020	Ethical Conflicts
ET Section 102.01	Integrity and Objectivity	1.100.001	Integrity and Objectivity Rule
New		1.100.005	Integrity and Objectivity - Application of the Conceptual Framework for Members in Public Practice
ET Section 102.03	Conflicts of Interest	1.110.010	Conflicts of Interest
ET Section 191.186-.187	Service on Board of Directors of Federated Fund-Raising Organization	1.110.010.01 j	Conflicts of Interest
ET Section 191.198-.199	Member Providing Services for Company Executives	1.110.010.01 k	Conflicts of Interest
ET Section 191.220-.221	Member is Connected With an Entity That has a Loan to or From a Client	1.110.010.01 l	Conflicts of Interest
ET Section 191.170-.171	Bank Director	1.110.020	Director Positions
ET Section 191.226-.227	Acceptance or Offering of Gifts or Entertainment	1.120.010	Offering or Accepting Gifts or Entertainment
ET Section 102.02	Knowing misrepresentations in the preparation of financial statements or records	1.130.010	Knowing Misrepresentations in the Preparation of Financial Statements or Records
ET Section 102.05	Subordination of judgment by a member	1.130.020	Subordination of Judgment
ET Section 102.07	Professional Services involving client advocacy	1.140.010	Client Advocacy

Test Your Ethics IQ – again wagering is OK

- An entity has engaged a CPA firm to perform agreed-upon procedures (AUP) related to royalty and licensing fees under Statements on Standards for Attestation Engagements (SSAE) No. 10 (as amended by SSAE No. 11), *Agreed-Upon Procedures Engagements*. The entity believes it is not receiving all the royalties and licensing fees it is due. The company has asked to pay the CPA firm based on a percentage of royalties and licensing fees collected. The CPA firm currently provides only tax services to this entity. A 3rd party is not expected to use the report. May the CPA firm perform this AUP engagement on such a contingent-fee basis?

Test Your Ethics IQ – again wagering is OK

- A CPA firm has acquired a new client. The client's financial records were prepared by the predecessor CPA firm in QuickBooks. Is the predecessor CPA firm required to provide, upon the client's request, the client's records in a QuickBooks data file to the client?



Test Your Ethics IQ – again wagering is OK

- A manager of a CPA firm provides more than 10 hours of consulting services to an attest client of the firm. The manager's spouse is employed by the client in its engineering department (a non-key position). The client requires that all matching of 401(k) contributions be made with the company's stock. Can the manager's spouse participate in his company's 401(k) plan without impairing the CPA firm's independence?



QUESTIONS

Our New Address in Pasadena

**221 East Walnut Street,
Suite 260**

**Pasadena, California,
91101**

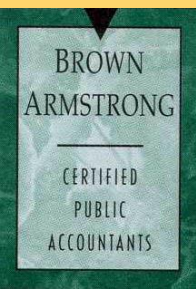
**Phone - 626-204-6542
extension 701**

Fax - 626-204-6547

Mobile - 626-375-3600

Email:

eberman@bacpas.com



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